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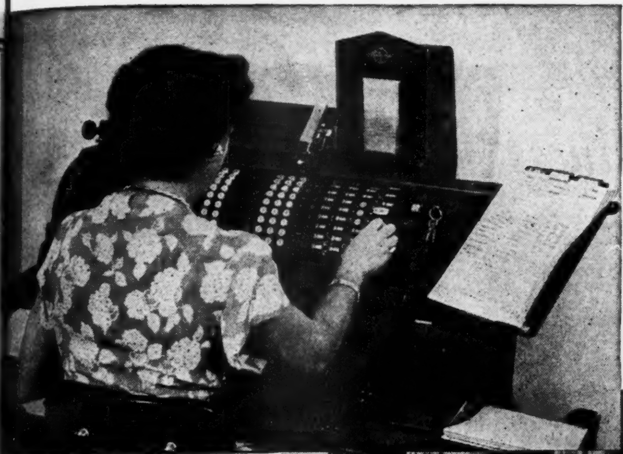

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# THE NEW YORK CERTIFIED PUBLIC ACCOUNTANT

EMANUEL SAXE, *Managing Editor*

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# The Auditor's Duty Regarding Fixed Assets and Capital Accounts on a First Audit of an Established Firm


*By* ARTHUR W. HOLMES


ON his first audit of an established business organization, the accountant realizes that he must render an opinion as expert as if he had been examining the accounts of that client for a number of consecutive years, or from the date of the inception of the business. Because it is his first examination of an established company, the accountant's responsibility is in no way lessened for a proper presentation of balance sheet condition and operating results.

The rendition of an expert opinion for a new client who has been in existence for a number of years presents problems and additional work for the accountant so that he may be satisfied not only with accounts which primarily are current in nature, but particularly with the corrections of

(a) The fixed tangible assets,

(b) The fixed intangible assets, and

(c) The capital accounts of the business.


ARTHUR W. HOLMES is Associate Professor of Accounting in the College of Business Administration, of the University of Cincinnati. He is the author of *Auditing: Principles and Procedure* and other texts on accounting. He is also engaged in private practice and is a director of several corporations.


The audit procedures for the remaining accounts—the majority of which are of a current nature—are not materially affected by the fact that this is a first examination of an established company; this is true due to the fact that opening balances may be verified, and current transactions examined to determine the results of operations for the period and account balances at the end of the year.

### The Fixed Tangible Assets

The problems of the accountant with respect to fixed tangible assets in his first examination of an established firm may be classified (1) as those pertaining to the accuracy of the gross carrying value of each asset and (2) as those pertaining to the accuracy and reasonableness of the net carrying value of each asset.

The accuracy of the gross carrying value of each asset is dependent upon the correctness of original cost—or other acquisition—figures, the accuracy of the distinction between capital and revenue expenditures as fixed tangible assets are acquired, and the accuracy of

charging off fixed tangible assets which have been disposed of or fully depreciated.

The accuracy of the net carrying value is dependent upon the accuracy of the gross carrying value minus the depreciation charged off and the accuracy of the charge-off of fully depreciated fixed tangible assets and those disposed of by sale or other methods. The determination of the accuracy of past accounting for gross and net carrying value of fixed tangible assets is the primary responsibility charged to the auditor on a first examination of an established company.

In a first audit, the accountant must display good judgment and discretion with respect to the extent of the analyses to be made in order to establish the accuracy of the asset values—gross and net—at the date of the current balance sheet. To indicate that each fixed tangible asset account must be completely analyzed from the inception of the business would be not only ridiculous, but in many instances impossible. A general and inflexible rule cannot be formulated for fixed tangible asset procedure on a first audit. The procedure for each asset is suggested in the following sub-sections of this section.

*Land*

The accountant is charged with the responsibility of satisfying himself concerning the ownership of the land and with the responsibility of determining the method of acquisition and the reasonableness and accuracy of the carrying value of the land. On a first audit, the accountant should request and obtain a confirmation of ownership from the client's attorney or from the title guaranty company. This confirmation, when obtained, should become a part of the accountant's permanent file for that client. In lieu of requesting an ownership confirmation, deeds and guaranty policies may be examined; also, tax bills prepared in the name of the owner may be examined as evidence of ownership. After determining the ownership of the land, on a first audit, the process requires no repetition in subsequent engagements, unless additional land is acquired.

In an initial audit, freedom from or the existence of mortgages on land must be determined, as well as existing judgments, taxes in arrears, and other liens. The confirmation obtained from the company attorney or title guaranty company should include the existence of mortgages and other liens. Mortgages and other liens should be set forth separately in the balance sheet, and should not be shown as deductions from land values.

Preferably, land should be carried at cost if it originally was acquired by purchase. The accountant should examine the original purchase contract, assuming that it still is available. If available, the minutes of the board of directors authorizing the purchase and the cancelled checks given in payment should be examined. Excerpts from these documents and records should become a part of the accountant's permanent file. It may happen that none of these records are available after the expiration of years, in which event the accountant must be satisfied with the continued carrying value over the years, at a constant figure.

If land originally was acquired by purchase at a price far below current replacement cost, it may be that after the expiration of years an upward appraisal of the land was justifiable. In such an event, the accountant should examine the appraisal report and satisfy himself with respect to its features, examine the minute book of the board of directors for the acceptance of the appraisal and examine the authorization to increase the value above cost, examine the capital reserve account credited at the time of the appraisal, and examine the disposition—if any—of the capital reserve account.

If land was acquired by gift, it should be valued at its appraised amount, which should bear the approval of the

board of directors, and it should be set up in the accounts only after all the requirements of the donor have been fulfilled. When land was acquired by gift, the auditor must feel certain that the appraisal was reasonable and that the client has free title to the property, not only so far as public records are concerned but also with respect to the requirements of the donor.

If land was acquired and paid for in the capital stock of the corporation, the land may be capitalized at the par value of the capital stock given in payment, or at the fair market value of the capital stock so given. Capitalization at the fair market value of the stock usually results in the more conservative valuation of the land; however, the decision of the board of directors will prevail, and the accountant is justified in accepting the reasonable conclusion of that body.

On an initial examination, the auditor's working papers for land should contain not only an analysis of the land account from the inception of the business (if this is possible and reasonable) but also full notes concerning the methods of acquisition, excerpts of deeds, excerpts of title guaranty policies, excerpts of minutes for purchase authorizations and appraisals, ownership confirmations, registration dates, notations of mortgages and their cancellation, and sketches of the plot or plots.

*Buildings*

On a first audit, the accountant should examine the authorizations for the purchase and/or construction of the buildings. He should obtain and examine all contracts, purchase orders, and vouchers, and he must vouch all payments made for the purchase or construction of the buildings for as many past years as necessary to verify the cost of the structures. Normally, buildings are not so old in the hands of the present owner, as to render this procedure impossible. If purchase price or construction costs have exceeded the amount of the authorization of the board of directors, approval for the excess cost should be called for and received.

Improvement of buildings and additions to them should be added to the cost of the buildings; extraordinary repairs and replacements should be charged to the reserve for depreciation; and ordinary repairs and replacements should be charged to current operating expense. Therefore, the accountant must examine expense accounts for past years to determine the accuracy and reasonableness of the distinction made between capital and revenue expenditures; in addition, he must examine the building accounts to determine that items properly chargeable to expense were not capitalized. This review will involve the examination of architects' estimates, contracts, purchase orders, and purchase invoices. The reports of the United States Treasury Department frequently will reflect light on the acceptance or rejection of expense charges which should have been capitalized.

By analyzing the buildings account and by following the suggestions of the two preceding paragraphs, the reasonable gross cost of the buildings may be determined.

The reserve for depreciation of the buildings should be analyzed from the inception of the business, or at least as far back as records are available, in order to determine the accuracy of the total balance in the account. Approval by the Treasury Department of past years' federal income tax returns will serve as a guide to the reasonableness at the top level of past annual depreciation.

While analyzing the reserve for building depreciation, charges to the reserve should be particularly examined to determine the propriety of and the reason for the charge. Charges normally result from the disposition of a building by sale or trade, its full depreciation, abandonment, destruction

by fire, or from adjustments for improper credits of preceding years.

In a first audit it is necessary to determine those buildings owned but used for other than business purposes; these should be removed from the fixed tangible asset classification and shown as investments or other assets in the balance sheet.

Buildings should be valued at cost minus the accumulated reserve for depreciation, or if this is not possible and reasonable, at appraisal value minus the accumulated reserve for depreciation. In a first audit, the accountant must examine all appraisal reports, the actions of the board of directors with respect to the appraisal, and the method of treating depreciation on the appraisal, both for account record purposes, and for income tax purposes. Liability accounts should be examined for evidences of liens on buildings.

The working papers on a first audit of buildings should be full, of course, and should contain, in addition to the customary analyses prepared in a repeat engagement, such data as: excerpts of authority to purchase, construct, and dispose of buildings; the verification of ownership; if purchased, the ascertainment of cost; if constructed, ascertainment that cost was properly computed; full notes on purchase orders and vouchers connected with the purchase of buildings; an opinion statement of the propriety of the distinction between capital and revenue expenditures; an analysis of the cost of additions and improvements; notes on examination of real property tax reports to ascertain that taxes were paid; computations of profits or losses on the sale of buildings and the reflection of the profits or losses in the statements of profit and loss and federal income tax returns; computations determining the correctness of annual amortization if buildings were erected on leased land.

*Machinery and Equipment*

In an initial audit of machinery and factory equipment, the first step should be a trip through the factory, learning the names and functions of the machinery and equipment. If a machinery list exists, or if it is possible to transport subsidiary machinery records through the factory, this should be done, and the machinery should be checked with the list or the subsidiary ledger accounts in order to become familiar with the machines and their records, and in order to determine record omission of machines in the factory.

In many engagements, due to the large number of machines, it is inadvisable to attempt to vouch all machinery purchases, but sufficient tests should be made to satisfy the auditor that all machines present are in the records at their proper acquisition figure. During an examination of machinery acquisitions of past periods, the accountant should exercise care to determine the disposition of such charges as transportation charges on purchased machines, installation costs, reinstallation expenses, and the costs of constructing machines for company use. The point of this section of the examination is to be certain that only proper items for capitalization are included in the accounts, and that the accounts contain all charges that should be capitalized. The deductions made from the accounts in past periods should be tested sufficiently to convince the auditor that they were properly made; if any such credits are improper, the accountant should prepare the necessary adjustments. Ordinary repairs and replacements should be charged to expense, and the accountant must ascertain that they have been so treated in past periods; extraordinary repairs and replacements should be charged to the reserve for depreciation if the life of the asset is thereby prolonged beyond the original estimate of life.

Subsidiary machinery account records should be reconciled with the controlling account at the beginning of the current period. Thus, having reconciled as of the beginning of the period

and having performed sufficient vouching of machinery acquisitions and dispositions of past periods, the accountant should proceed to analyze the machinery account for the year under audit; to do this, he should examine acquisition authorizations, and vouch machinery purchase orders, vendors' invoices into the machinery account in accordance with the procedure applicable to a repeat engagement.

The reserve for depreciation of machinery and equipment should be analyzed for several consecutive past years, and reports of the United States Treasury Department should be examined to ascertain acceptance or rejection of the depreciation provisions of the company. In addition, on a first audit, the accountant should determine if his client has taken advantage of the maximum depreciation possible in accordance with Treasury Department bulletin suggestions and in accordance with usage of the machinery. The depreciation policy should be consistent from year to year and the rates should be established in order to provide for obsolescence and inadequacy, in addition to normal wear. Provisions of past years should be thoroughly tested, and the general adequacy of the past annual provisions may be judged by reviewing the gains or losses upon disposition and retirement. When reviewing the reserve for depreciation, it should be borne in mind that charges to the reserve should appear only for corrections, dispositions, retirements, and extraordinary repairs and replacements.

It is generally accepted that machinery should be valued at cost minus accumulated depreciation; therefore, the accountant must be particularly careful to ascertain that cost has not been overstated or understated in past periods. These remarks apply particularly to machines and equipment constructed for company use, where manufacturing overhead may or may not have been added to material and direct labor cost.

The working papers prepared for machinery and equipment on a first audit should contain, in addition to the customary current analyses, answers to the following questions:

1. At what values are machinery and equipment carried? Cost? Appraisal? Cost minus depreciation reserves?
2. Are all additions and deductions properly authorized?
3. Does idle machinery exist?
4. What method of depreciation is employed?
5. Are reserves used or is depreciation credited directly to the asset?
6. Are depreciation reserves adequate?
7. Are depreciation reserves properly charged when machinery is sold, scrapped, or otherwise retired?
8. Is there a tendency to charge inexpensive machines to expense, at purchase?
9. Have depreciation rates been accepted by the United States Treasury Department?

*Perishable Tools*

During a first audit of the perishable tools account, the accountant should be particularly careful to ascertain that tools—useful for more than one year—are not charged to expense at the time of purchase. There has been a tendency to purchase tools heavily in profitable years, charge them to expense at purchase, and then absorb them physically over succeeding years. The accountant should ascertain if an annual tool inventory has been taken, priced, and reflected in the asset account for perishable tools.

If tool purchases are not large and if they have been charged to expense at purchase, and if tool purchases have been fairly constant in dollar volume from year to year, and if the omission of a tool inventory has no significant effect upon the assets or the expenses, there could be no objection to charging perishable tools directly to expense at

acquisition, if the practice was consistently followed from year to year.

A reserve for depreciation may or may not be maintained for perishable tools; this is a matter of individual company policy. If a reserve for depreciation exists, the accountant should analyze the reserve for a sufficient number of past years to satisfy himself of the accuracy and reasonableness of the reserve balance and the propriety of entering charges and credits in the account.

In summary, it may be said that the principal points in a first audit of the tools account are to determine company policy with respect to capitalization and expense, and to determine the accuracy of tool account balances at the beginning of the year under examination in terms of the relationship of the account balance to a physical inventory. From this point forward, the audit procedure would not vary from that of a repeat engagement.

*Other Fixed Tangible Assets*

The initial audit procedures for the remaining fixed tangible assets do not vary from the initial procedures indicated for machinery and equipment. Delivery equipment may be replaced more frequently than any other class of fixed tangible assets, tools excepted; therefore, on a first audit, it is particularly necessary to verify the accuracy of the entries made in past years upon the trade-in of old equipment for new, not only from the point of view of correct accounting procedure but also from the point of view of the accuracy of complying with federal income tax regulations.

In order generally to summarize the accountant's duties on a first audit of fixed tangible assets, the following procedures may be outlined for years preceding the year of current examination:

1. Determine the cost of acquisition, or other original capitalization figure.
2. Completely vouch or test-check additions, verifying cost or appraisal.
3. Completely vouch or test-check deductions.
4. Completely verify all fixed asset dispositions.
5. Examine depreciation reserve charges and credits.

**The Fixed Intangible Assets**

On a first audit of fixed intangible assets, the principal problem is one of determining the valuation originally and subsequently applied to these items in order to bring them into the accounts. There can be no debate of the statement that intangible values become recorded in the accounts by many means other than by purchase—a statement not generally applicable to fixed tangible assets. In addition, it also is true that intangible values frequently are changed after acquisition, and in many cases these changed values have resulted from whim rather than from reason. In connection with a first audit, one of the objectives of the accountant should be the promotion of sound and acceptable practices in the valuation of fixed intangible assets.

As a result of this primary objective, in an initial engagement it is desirable and necessary to analyze the accounts and verify all transactions back to the inception of each fixed intangible asset account in order to determine the cash or other value of the asset at the time of account creation, and in order to determine subsequent additions and amortizations, so that values may be expressed properly at the balance sheet audit date.

In connection with the verification of the origin of all intangible assets, care must be exercised to be certain that the accounts were legitimately created. No fixed intangible asset account should be the capitalized result of former operating losses, credits to capital accounts arising from the disposition of donated capital stock originally issued for an intangible asset, the charge-off of unpaid capital stock subscriptions, or the capitalization of corporate organization expenses. Accounts

with intangible assets have been known to serve as hiding places for expenses, or for the creation or inflation of values that should not appear in the balance sheet.

Whether the values of fixed intangible assets are large or small, absolutely, or compared with fixed tangible assets, the auditor should be exacting in his determination of original source, the conditions under which the intangible assets were brought into the accounts, the original costs, appraisals, and the provision for amortization if amortization is desirable or necessary. In many instances involving fixed intangible assets, it is difficult to assign a value to them, especially when that value is in excess of cost.

It might be mentioned at this point that the Securities and Exchange Commission requests the opinion of the accountant concerning the source and the reasonableness of the values of fixed intangible assets. In addition, the Commission insists upon the assignment of reasonable values to intangible assets. In the registration statements, intangible asset values must be given full disclosure in order to attempt to avoid a reflection of inflated asset and capital values in the balance sheet.

In addition to verifying source, cost, appraisal, and amortization of fixed intangible assets, the advisory duties of the accountant for this class of asset covers a wide field. The accountant must remember that the present and future interests of present and future owners must be protected and, consequently, if intangible fixed assets are not soundly treated, invested capital may be jeopardized. For all fixed intangible assets except goodwill, documentary evidence of cost, appraisal, etc., should be available for the auditor.

The working papers for fixed intangible assets should start with the creation of each intangible asset account, and should detail each charge and each credit, both for dates and amount and the reasons for the entries. The reasons for the charges and credits should be fully annotated and reference made to the original documentary evidence of the client. Ownership must be verified and all documents must be read, and understood. Vouchers and all other evidence of transactions giving rise to account charges must be fully examined and the entries traced to the accounts. Verification must be made of the amount and correctness of and the authority for all entries reducing fixed intangible asset accounts, from their inception, and the accountant must determine that the debit was correct when an intangible asset account was credited.

When fixed intangible assets are carried at other than cost figures, the accountant must consult company officials to assist in his determination of proper and reasonable valuations.

The initial audit procedures for a few typical fixed intangible assets are presented in the following sub-sections.

### *Patents*

In the first audit of patents, the patent letters issued by the United States Patent Office should be read and excerpts of importance taken from them. If the accountant is in doubt as to whether a patent is owned or leased, he should request a confirmation from the attorney of the client. Vouchers and other evidence proving original cost should be examined and traced to the patents account. If patents were developed by the client, all research costs, experimental expenses, legal fees, patent fees, and other development costs should be audited in reasonable detail to determine the legitimacy and correctness of the capitalization of the expense outlays. Development expenses which did not result in the acquisition of a patent should not appear in the asset account.

A patent always is a questionable asset until it has been subjected to a lawsuit brought by someone honestly interested in establishing his priority. Therefore, the accountant should prepare full notes in his working papers

of all lawsuits and their results. Amounts spent in infringement suits in title defense may be added to the patents account, if desired, providing the suit has been won.

Patents should be amortized over the shorter of their legal life or their expected productivity. It is always advisable to conservatively estimate the expected productive life, and in a first audit the accountant must discuss these productive possibilities with the client. Patents which are not productive of income either because they were purchased and placed on an inactive status or because there was no demand for the product manufactured under the patent, should be charged out of the accounts.

The patents account should be analyzed in detail back to the oldest patent remaining in the account. Every debit in the account should be tied in with the cost of one of the patents, and charges not allowable to a specific patent should be removed from the account. It may happen that a productive patent has been appreciated in value in the account, with an offsetting credit to a surplus account, other than earned surplus. If the productivity of the patent was such that the appraisal met with the approval of the accountant, the balance sheet should be annotated, explaining the situation. After analyzing the patents account for all past periods, the audit for the current year should proceed in the customary manner.

### *Good Will*

In a first audit of good will, the major problems are the determination of the basis for the existence of a good will account, and the analysis of its valuation. The creation and the valuation of the good will should be completely detailed on the accountant's working papers. The accountant should bear in mind that good will has no value in the event of liquidation, and that therefore it should appear in the accounts at no greater amount than the price paid for it upon the acquisition of a business for cash, capital stock, or other valuable consideration. The price paid for good will normally represents the excess of the purchase price over the net worth of an acquired company. If the good will account arose from a merger of several companies of different earning power, it would not be necessary to show a good will account if capital stock of no-par value was used in the financing.

All accountants agree that good will should not appear as an asset unless it was purchased in the acquisition of a business, or unless it resulted from a merger. All accountants do not agree to the amortization or non-amortization of good will; this is a matter of personal opinion. Good will fluctuates in value from year to year, just as fixed tangible assets fluctuate in market value. Unless the good will has been lost or has permanently declined in value, it need not be amortized. If the desire is to amortize the account, the amortization should be on an inflexible basis, with the offsetting charge being made to the earned surplus account.

### *Other Fixed Intangible Assets*

The duties of the accountant in a first audit of trade-marks, copyrights, and franchises do not differ from his duties as explained for patents and good will. Trade-marks usually are registered, and because they have no maximum legal life, it is not mandatory to amortize them providing they are productively employed. If trade-marks are not in active use, they should be charged off, or reduced to a nominal amount. The accountant must exercise care to ascertain that trade-mark values have not been inflated and transferred to a good will account, and he must read and extract notes from the registration letters and from the correspondence with the client's attorney.

Copyrights should not appear in the accounts in excess of cost, and they should be amortized rapidly. The best procedure is to ascertain that the cost

of the copyright has been charged to the first production of the copyrighted item.

In a first audit of franchises, the accountant must investigate the franchises to familiarize himself with the terms of the grant, including such features as restrictions imposed, fees, rentals, the right of the grantor to assume operations in the event of specified contingencies, revocable features, rate clauses, service clauses, and maintenance provisions. The auditor must examine the franchise accounts to ascertain that they have been carried at cost less proper amortization if the franchises were acquired by purchase. If the franchises were acquired without cost, no values should appear in the account, and rentals should appear as operating expenses. The auditor must determine the adequacy or inadequacy of periodic amortization charges for franchises of limited life and for franchises containing revocable clauses. After this preliminary work, the audit would proceed along the pattern of a repeat engagement.

## The Capital Accounts

The capital accounts refer to all capital stock accounts, surplus accounts, surplus reserve accounts, and if the client is other than a corporation, to the permanent capital and drawing accounts of the proprietors.

In an initial engagement, the accountant must familiarize himself with, and ascertain that the client has adhered to, the legal requirements of the state of incorporation relative to such matters as incorporation procedure, securities qualification, the issuance of capital stock at a discount, the minimum amount per share for which no-par value capital stock may be issued, regulations pertaining to the acquisition or non-acquisition of treasury stock, the maintenance of stockholders' records, requirements for minimum paid-in capital, laws concerning capital stock dividends, and other requirements of the state and its political subdivisions.

### *Capital Stock*

In a first audit of a corporation, the accountant must examine the certificate of incorporation, and any amendatory certificates, noting all matters affecting the accounting and the audit, such as the precise names of the classes of capital stock, the number of authorized shares of each class, the par value per share of each class, the callable features of each class, and dividend specifications.

The minute book of the board of directors and the corporate code of regulations should be read and notes made to determine corporate policies and activities concerning: authorized increases, retirements, new issues of capital stock, the creation of reserves, the retirement of reserves, dividend actions, cumulative and participating features of preferred stock, redemption fund provisions, callable features, and other priorities of preferred stock in the event of dissolution. The authorizations of the board of directors must be examined to ascertain that the proceeds of capital stock sales were applied in conformity with the authorizations if restrictive stipulations were inserted at the time of issuance.

Each capital stock account must be analyzed from the beginning of the business in order to determine the correctness of the balance at the beginning of the year under examination. This means that the examination shall cover all increases in capital stock and the verification of the offsetting debit, and all decreases in capital stock and the verification of the offsetting credit. All journal entries opening capital stock accounts should be reviewed to ascertain that they are correct and that they result in the proper reflection of capital stock in the balance sheet.

The treatment accorded premiums and discounts on the sale of original capital stock issues must be examined. If capital stock has been issued at a discount, and had not been fully paid at a subsequent date but was described as fully paid, the accountant must be

certain that there was no violation of a state law. If capital stock was issued at a premium or at a discount, the balance sheet should show these facts unless the premiums and discounts were written off to a surplus account by authorization of the board of directors.

Subscription agreements should be inspected, and when the subscriptions account was credited the offsetting charge must be traced to be certain that subscriptions were not written off without the receipt of payment. Directors may become personally liable for authorizing the cancellation of unpaid subscriptions. Subscriptions in arrears should be investigated and comments prepared.

The audit then will proceed in the usual manner for a current examination.

If the capital stock is of no-par value, the accountant must examine the records to determine the consistency of carrying the capital stock at (1) the amount of the consideration received for it, (2) its stated or declared value, or (3) no value. If (2) or (3) represents the method followed, the accountant must ascertain that the proper surplus — paid-in surplus — was credited. The laws of certain states stipulate a minimum issuing price per share for capital stock of no-par value. When laws of this type exist, the auditor must verify the records to determine that the amounts credited to the no-par value capital stock account have not fallen below the required minimum.

*Earned Surplus*

Earned surplus should be analyzed, if reasonable, from the inception of the account. The auditor must ascertain that entries in the earned surplus account properly belong there and not in other accounts, particularly other surplus accounts. The sources of the earned surplus account should not only be analyzed on the working papers, but full notes concerning the account should be made. The propriety of the sources must be above question, and, for example, should not be the result of reductions in the par value of capital stock, or intangible and tangible asset appreciation. Charges to earned surplus of past years should be properly supported by action of the board of directors for such items as dividends and surplus reserve creations. The propriety of earned surplus can be ascertained only if it is proven that surplus reserves have been accounted for properly in past years; this involves an examination of all earned surplus reserves.

*Capital Surplus*

The capital surplus account should be analyzed from the inception of the business, and all charges and credits should be fully explained in the working papers. All reasons for charges and credits to the account made in past years should be fully understood, and their propriety and accuracy approved.

The auditor must be familiar with the laws of the state of incorporation to ascertain the permissibility of recording in the capital surplus account such transactions as the payment of dividends and particularly the payment of dividends if the earned surplus account is not sufficiently large to cover the dividend.

*Paid-in Surplus*

The paid-in surplus account should be analyzed from the beginning of the business, and it should contain only transactions connected with the capital stock of the issuing corporation. The accountant should watch particularly to determine and understand the source of the account and to determine that the account was not used to absorb losses of early years of operation. The accountant must remember that the paid-in surplus account represents originally invested capital. All entries affecting the account should bear the approval of the board of directors. Many states do not prohibit dividends—cash or stock—from paid-in surplus, and consequently the accountant must verify the legality of the use of the account. After an earned surplus account has

been accumulated, the paid-in surplus account may be transferred to earned surplus, but if this action was taken the board of directors should have reserved a portion of earned surplus equal to the paid-in surplus so transferred.

### *Donated Surplus*

Donated surplus, like paid-in surplus, constitutes a part of the invested capital, and should not be made available for dividends unless it was specifically donated for that purpose. The donated surplus account must be analyzed from the beginning of the business. The accountant must verify the sources of the donated surplus account, must understand the terms and conditions of the donation, and comment upon donations when donated assets were overvalued. If treasury stock donations were credited to the donated surplus account, the account should be charged if the donated treasury stock later was sold at a discount.

The auditor must examine the records for exchanges of capital stock for assets, with a portion of the same capital stock being donated back to the corporation. Obviously the assets were acquired at inflated values, and the assets should be devalued in accordance with the reasonable value of the stock donated back to the corporation.

### *Reappraisal Surplus*

Reappraisal surplus should be analyzed from the inception of the business, and all sources of the account should be verified. The initial audit of this account usually is made in connection with the examination of the assets which gave rise to the reappraisal surplus account; however, a few remarks are presented at this point.

In connection with the first audit of the account, the auditor must ascertain that depreciation expense has been computed on the cost of the assets and that the reappraisal surplus account has been charged with the amount of the depreciation on the appreciation, or that depreciation has been based on gross appraisal value and the reserve for depreciation credited in full, in which case a transfer entry would be made transferring from reappraisal surplus to earned surplus an amount equal to the depreciation on the appreciation. The accountant's working papers should contain full explanations of the sources and uses of the account, and he should remember that appraisals of depreciable assets reflected in the account must be completely eliminated upon the disposition or full depreciation of the appreciated assets.

### *Surplus Reserves*

All surplus reserve accounts should be analyzed from the inception of the accounts. The auditor must ascertain the authority for the creation of each such reserve. He should then determine the purpose for which the reserve was created and ascertain whether the creation was voluntary or involuntary. If the creation of the reserve was obligatory, the necessary contracts and agreements must be examined to determine that the provisions thereof have been followed and that the reserves are of proper amount. The reason for the creation of any surplus reserve must still exist at the time of audit, regardless of whether the reserve was voluntarily or involuntarily created. If the reasons for the amount of any particular reserve are not clear, the amount of the reserve and the reasons for its existence should be discussed with the client in order to clarify the financial statements and the audit report.

### *Partnership Capital*

In the initial audit of a partnership, the auditor must read and extract notes from the articles of copartnership for such items as capital contributions, salaries, interest credits on capital, interest charges on drawings, the profit and loss sharing ratio, dissolution arrangements, and all other matters of importance. He must be certain that

past violations of the partnership agreement do not exist at the time of the first audit.

Each capital and drawing account must be analyzed from its inception, or, if this is unreasonable, for a number of past years sufficient to result in accuracy of balance at the beginning of the year of examination. If dissolutions have taken place in the past, followed by the formation of a new partnership, the accuracy of the dissolutions should be verified in order to avoid future complications.

## Bookkeeping Records in Venezuela

Venezuela is quite a country, especially from an accounting point of view.

Each book of account must be a bound book; each page of the book must be stamped with an official stamp; and on the first page the bookkeeper ("Accountant" down here) must write the use of the book and the date it was acquired. No entries can be made in the book dated prior to its acquisition.

The two legally required books are a "Diario" (Journal), and a "Major" (General Ledger). It is illegal to make any alterations or erasures in either of these books. Everything including Cash must be entered through the "Diario", though a "Caja" (Cash Book) is usually kept and the Cash summary is journalized at the end of the month.

The severe prohibition against alterations leads to some very peculiar adjustments such as entries without a source, or purposely-created errors to compensate for prior errors.

The conduct of the books is covered by the Commercial Code and is very strict since in case of a question as to the owing of a debt, etc., the books constitute legal proof unless specifically proven wrong.

All bookkeepers are known as "Accountants". Professional accounting is just being born in Venezuela.

CHARLES M. HECHT, C.P.A.,
of Charles Hecht & Co.

# Some Fundamentals of System Design

*By* H. K. Marks, C.P.A.

## Opportunities in Systems and Procedures Work

ACCOUNTANTS are presented with a unique opportunity in the field of systems and procedures design. This specialization falls peculiarly within the scope of the accountant's activities, and rightfully belongs in the hands of men who are bound by a code of professional ethics and practices.

Never before has American business been so in need of competent advisers in this field. Because of the unusual demands made by the war, numerous requirements of government regulatory bodies, and a myriad of other reasons connected with mass production of wartime products, systems in manufacturing and commercial businesses were so altered, remodeled and designed as to bear no proper resemblance to the methods which should be employed in peace-time operations. Moreover, businesses which remained dormant during the war because of their non-essential character, scarcity of materials and other reasons, are now springing to life under new and changed economic conditions. This is a tremendous challenge to the accountant's ingenuity, a test of his adaptability to changing circumstances.

System design requires a thorough basic knowledge not only of accounting precepts, but also of the tools with which the administrative personnel of all businesses must work for maximum efficiency. Strangely enough, in the past, very few accountants have seen fit to specialize in this important phase of professional activity and have left most of this work to non-professionals. The field, therefore, is far from overcrowded and provides one of the most advantageous fields of endeavor to the returning veteran with excellent opportunities for remunerative return.

H. KENNETH MARKS, a partner in the firm of J. K. Lasser & Co., is a Certified Public Accountant of New Jersey and California, and is actively engaged in the fields of systems, management, audits and taxation. He is the National President of the Systems and Procedures Association, a member of the faculty in the Division of General Education at New York University and of its Institute on Federal Taxation. He is also Chairman of the Committee on Federal Taxation of the New Jersey Society of C.P.A.'s.

This paper was presented by him as one of the lectures in the Review and Reorientation Course sponsored by the New York State Society of C.P.A.'s for its veteran members.

## Approach to the Subject

Unfortunately, there is no really comprehensive bibliography on the subject of systems and procedures. Some few organizations have attempted to form study groups to explore the field. In most cases, discussions have followed the "illustrative case" pattern, whereby people who are engaged in every-day system design, describe the routine and method under which a particular operation, such as billing or purchasing, is performed. While this form of study may be interesting, there is grave doubt in my mind that it provides any real benefit to the systems student. No system, however perfect, may be transferred lock, stock and barrel from one company to another, since the elements of system design are such that the requirements of no two companies can be precisely alike.

In this discussion, I have sought to approach the subject from a different point of view, that of resolving a system into its three essential elements in

the light of results which it is designed to achieve. These basic elements may be classified as follows:

1. The methods *of recording* business transactions with maximum efficiency.
2. The methods instituted in order properly to *control and protect* the company assets.
3. The methods instituted for the purpose of reporting to management in the form of Profit and Loss Statements, Balance Sheets and other statistics, and the interpretation of these reports.

### Accounting Systems

What is an accounting system? It may be said that accounting itself deals with the systematic recording and interpretation of business transactions and that the techniques used in recording business transactions are known as bookkeeping, whether single entry or double entry.

But the concept of systems and procedures contemplates a much broader field encompassing not only the result but, particularly, the method by which it is achieved. In the design of a system it is important that we always bear in mind the three distinct elements, enumerated above.

Individual treatment will, of course, vary with:

1. The volume of transactions in the company,
2. The location of the various plants, branch offices and other material factors, and
3. The extent of the detail required.

If an over-simplified summary can be justified for the purpose of clarity, accounting systems may be said to embrace four basic functional operations:

1. Cash receipts.
2. Cash disbursements.
3. Purchases of merchandise or services.
4. Sales or other income-producing activities.

Numerous related records are created in the system design which will be discussed at the appropriate time, but basically, these four functions constitute the major problems with which system design is concerned.

### Systems of Recording

At the outset, it would be well to consider the general nature of recording problems.

Fundamentally, double entry bookkeeping employs only two basic records:

1. Books of original entry, called journals.
2. Books of secondary entry, called ledgers.

Actually, the problem of recording could be simplified even further by dispensing with the use of journals and making entries directly to the ledger accounts. Obviously, however, this would give rise to a whole host of objections with which all accountants are familiar.

Essentially, all entries for a business could be recorded in these two basic records, but naturally, the procedure in a company with a large volume would be slow and cumbersome. It is for this reason that we have watched the evolution of additional records all of which nevertheless fall within the above two basic categories. Briefly, books of *original entry* have evolved in the following manner:

1. The columnar journal with separate columns for the entry of cash, purchases, sales and other items, permitting the posting of totals, instead of details, to the books of secondary entry.
2. Separate journals for cash receipts, cash disbursements, purchases, sales, credit memos and the like. These may, likewise, be columnar in form to permit further analysis of items of original entry.
3. The simultaneous preparation of journal and ledger sheet com-

monly found in some machine bookkeeping systems where, for example, the posting of sales or cash receipts to the customers' accounts is carbonized to a journal sheet.

4. The complete elimination of journals in favor of summary entries. This is commonly found today, for example, in the filing of copies of sales invoices, the totals of which are posted to the books of secondary entry.

As mentioned before, all classifications of accounts could be maintained in one ledger, but this, too, would be cumbersome and unwieldy in a large company. For this reason, we have seen the evolution of recording in books of *secondary entry* in the following manner:

1. The posting of summary totals instead of the details of the original entry. This follows the use of columnar books of original entry.
2. The use of separate subsidiary ledgers such as accounts receivable, accountants payable and factory ledgers; note registers; and similar subsidiary books.
3. The elimination of ledgers entirely, such as the use of copies of the invoices for accounts receivable, and the use of voucher registers to eliminate accounts payable.

## Systems of Control Over Company Assets

Controls may be either external (such as outside audits) or internal (which may or may not include an internal auditing department). In the design of systems, we usually concern ourselves with the problem of internal control although the value of an external, independent audit should not be overlooked in designing a system.

Fundamentally, internal control is usually centered around the principle of check and balance. That is, one person performs one part of the function and another person performs another part of the function. Thus, no diversion of the business assets can occur without collusion. For purposes of simplicity, these controls may be loosely classified as accounting and non-accounting controls.

Non-accounting controls include such devices as the following:

1. Two signatures on checks.
2. Bonding of key employees.
3. The writing of collection letters by persons not connected with accounts receivable bookkeeping.
4. Supervisory approval of changes and erasures on original documents.
5. Approval of expense and other disbursements by persons in authority.
6. Evidence of competitive bids on purchases.

Accounting controls include such devices as the following:

1. The segregation of the *handling* and deposit of cash receipts from the *accounting* for such cash receipts. One common example of this is the separate cashier's cage to receive and deposit money, and a different group concerned with the posting of accounts receivable.
2. The segregation of the disbursing of cash from the accounting for such cash disbursements. Thus, we have the accounting department computing payrolls, the actual payment of which is made by the paymaster.
3. The whole gamut of general ledger controls for other assets of the company, such as inventories of raw materials, work in process, finished goods, supplies, accounts receivable and so forth.

## Systems of Reporting and Interpretation

In general, as far as accounting systems are concerned, the major problem

is one of classification and analysis. These involve reports on such things as:

1. Departmental profit and loss statements and other statements and statistics required by management.
2. Budgets on future operations, cash forecasts and the like.
3. Sub-analysis of special items such as sales by territories, products, or salesmen.
4. Last, but not least, the preparation of the various reports required by governmental agencies such as Income Tax returns, Sales Tax returns, Withholding and Social Security Tax returns and the multitude of other reports required by Government.

The plethora of data which may be required by any individual company and the use to which it is put precludes any detailed discussion of practices with respect to the kind and frequency of these reports. But I caution all those engaged in system design to remember one very salient fact: Reports are wholly inanimate things, and they are only important if they are actually *used* by the people to whom they are submitted.

In general, analysis may be secured in one of two ways:

1. Through the establishment of predetermined accounting controls, such as departmental or divisional income and expense controlling accounts. Accountants are to be criticized for employing these devices in a great many instances where they are not required.
2. Analysis can also be secured through "memorandum" breakdown of basic documents and other records and, in proper system design, this method is much more flexible than the establishment of accounting controls.

In general, the secret of speed and economy in these tabulations lies in one act: planning. The planning should aim to avoid, as far as possible, the retabulation of the same items and to employ the use of rapid sorting systems. Retabulations may be avoided in a great many cases by the use of subsummaries which should be interpolated in the tabulation sequence where-ever their use in subsequent analysis is indicated, thus saving the time and avoiding the errors involved in a retabulation of the original documents. To illustrate with a simple example, we may assume a company desires a tabulation of sales for each salesman, territory, and division, as well as the total sales of the company. Obviously, the steps to be followed are:

1. Tabulate sales by salesmen.
2. Discard the orginal records and summarize salesmen's sales by territories.
3. Discard the tabulation of sales by territories and summarize sales by divisions.
4. Total the sales for all divisions to get the grand total of all sales.

## Approach to System Installation

It is vital to the efficient and economical installation of an accounting system that the problem be approached with the following thoughts foremost in mind:

1. The study of the end results desired in each of the three major categories discussed: recording, control and reports.
2. The separate cost of attaining each of these objectives.
3. The functional approach to each recording operation (cash receipts, disbursements, purchases and sales) bearing in mind the principles underlying each of these problems.

In other words, accounting systems are like cocktails, in that it is necessary

and important to employ proper ingredients and skillful blending for the best results.

### Hand Methods Versus Machine Methods

Too many accountants and business men assume that a machine is faster and more accurate than hand methods *per se*. In a great many cases, this is wholly untrue.

For example, let us take the simple addition of a column of figures. If it were necessary to write the figures to be added on a piece of paper by hand and then to add them, both of these operations could be done simultaneously and, therefore, faster on an adding machine. If, however, the figures are already written, properly trained employees frequently can add faster and more accurately than a machine. It is necessary to use more or less skillful hands to depress the keys upon the adding machine, and errors are often made in the process. To put it succinctly, there is more accuracy in the mind than in the fingers.

Or, take a simple posting operation on any standard bookkeeping machine. Anyone who has had real experience with posting operations knows that hand posting of individual items is considerably faster than machine posting of the same items. A simple time study will prove this to sceptics. Recent studies made by me, where one or two items were posted to individual accounts at a time, showed that 75% of the posting time was spent in

1. Locating the ledger card,
2. Inserting the ledger card, and
3. Extracting the ledger card.

In hand posting, of course, there is no inserting and extracting operation.

However, machine posting does attain superiority over hand posting in many cases for the following reasons:

1. Automatic balancing is provided. This is really a minor point because it requires machine pick-up of old balances and the throwing of new balances at each posting operation.

2. The simultaneous preparation of statements and ledger cards, and in some cases, simultaneous preparation of journals. However, statements and ledger cards can be prepared simultaneously by hand methods, also.

3. A machine will produce neater records and statements.

4. The use of machines permits the employment of lower-grade personnel because of the mechanical operation.

5. The machine produces an automatic proof of total postings.

### The Operational Approach

The system designer must always remember that basically, business operations are concerned with only two things—income and expenditures. In fact, if books were maintained on a cash basis, we would really be concerned only with cash receipts and disbursements.

Because of the more common use of the accrual method, however, we must also consider:

1. The purchase of goods or services and, therefore, related problems of accounts payable, etc.

2. Charge sales and, therefore, the related problems of accounts receivable, etc.

If you will just stop to think, you will discover that all additional related operations stem from these original sources, whether in the form of subsidiary records and statements and whether hand or machine methods are used. Let us now consider some of the problems.

### Sales and Accounts Receivable

In this brief paper, I have time to give only some of the basic principles underlying the systematic recording of sales which are universally applicable. The form in which these principles are

applied may vary, depending upon specific situations encountered.

*CASH SALES*—It is necessary continually to bear in mind the principles earlier enunciated, the fact that the complete system deals with three separate problems, viz.,

1. Recording,
2. Control, and
3. Reporting.

Generally speaking, no special devices are necessary to *record* cash sales in one total figure. Cash received represents such sales. Moreover, if general classifications of cash sales are desired, for example, drugs, cigarettes, soda fountain, this may be accomplished by separate cash drawers.

Individual sales books are sometimes used for

1. Instances where it is desired to give the customer a detailed receipt.

2. Cases where detailed cost records or perpetual inventories are in effect.

3. Internal control purposes, as where a separate wrapping desk is maintained. This is usually prevalent in retail stores.

*CREDIT SALES*—The main differences between credit sales at retail and wholesale lie in the method of delivery of the merchandise, i. e. at the point of sale (commonly encountered in retail stores) or by shipment to the customer. For this reason, in retail stores, it is necessary to prepare sales slips for the customers' signatures and, in addition, for the purpose of charging the items to accounts receivable. However, the recording problems are essentially the same. The major items to be considered in connection with sales are the following:

1. *Form design*—The form should be of a convenient size and shape and preferably of the smallest size convenient to accommodate the average amount of information and the average number of items. A number of basic principles should be closely watched in form design—

a. Avoid the writing or typing of unnecessary information. While this may seem an obvious exhortation, here are some things to refresh your memory:

i. Date stamp the date upon the invoice or use a date slug on your billing machine.

ii. Wherever possible, abbreviate or code the items appearing upon the invoice.

iii. Do not type any shipping instructions upon the invoice form unless the shipment is controlled by a copy of the invoice or it is necessary for the purchaser to be advised of the manner in which the merchandise was shipped.

iv. Do not insert the salesmen's name, territory or other similar information unless the invoices are being used for analysis or sorting. If a copy of the invoice is used for this purpose, code salesmen and other information.

v. If one discount applies to all items, try to show the calculation in one figure at the bottom of the invoice.

b. Be sure that the spaces on the invoices are conveniently arranged. It should be borne in mind that the cost of a form is the *completed* cost, not merely its printing cost. Watch for these things:

i. Be sure that horizontal alignment is carefully planned if both the left and right-hand sides of the form are typed, so that it is only necessary to tabulate to the proper position on the right-hand side of the form instead of turning the platen up and down.

ii. Be sure that vertical alignment is carefully planned so that the form may be filled out with the minimum of typewriter marginal stops. As a point of information, at least one typewriter company

has a return mechanism device which returns the form halfway instead of the full width of the typewriter.

c. Avoid carbon insertion, if possible, through the use of snap-out carbon forms, spot carbon, fanfold or continuous forms.

2. *Methods of Completing the Form*—The ideal method is, of course, to prepare every needed document at one writing by including a sufficient number of copies of the invoice. As a suggestion, at least these following items may be prepared simultaneously:

a. The invoice or invoices,

b. The accounts receivable copy,

c. The sales record copy (file copy), and

d. The sales analysis copy.

In designing the method, efforts should be made to include in this typing:

a. A label for the package,

b. The packing slip, and

c. The perpetual inventory or cost copy.

These objectives are sometimes difficult to achieve. If, for example, a whole set of invoices is typed at one time complete with extensions, it may be found that some of the merchandise is out of stock, which requires the return of the whole invoice set for correction.

On the other hand, if shipments of merchandise are made from the original order as received, it becomes necessary to prepare a label and packing slip in the shipping department. Then, when the order is returned for billing, all other copies must be prepared.

One economical solution is to have a billing division in juxtaposition to the shipping department. The original orders can be passed to the shipping department and the following operations performed:

a. The merchandise is gathered and items out of stock indicated upon the original order form.

b. The merchandise is laid out for wrapping.

c. The order is then passed to the billing clerk who prepares all necessary copies, including the label and the packing slip. If postage or other shipment charges are to be added, this information can be indicated upon the original order so that it can be inserted upon the invoice.

d. The label and packing slip are then returned to the shipping clerk who locates the laid-out merchandise and completes the shipment.

Another *economical* method is to ship from the original order without the packing slip and to invoice later. This merely requires the extra operation of preparing a label.

Usually, the least economical method is to type the invoice sets without extensions and to reinsert the invoice sets after the shipment of merchandise. This method, however, is necessary in some cases and is advantageous where control is sought since pre-numbering of the invoice permits the billing department to ascertain that all shipping instructions have been carried out.

3. *Methods of Original Recording*—The methods of recording sales have passed through a period of evolution in recent years. Let us follow that evolution:

a. The Sales Register in which the individual sales invoices were listed with the name of the customer and the amount.

b. The columnar register in which columns were provided for the analysis of sales.

c. Copies of sales invoices for each day only, the totals of which were entered in a sales journal, the invoice copies being retained in binders to support these entries.

It is important to note that as our experience with recording problems

grows, progressive accountants seek, more and more, to avoid the detailed transcription of entries.

4. *Methods of Posting* — Posting methods, too, have gone through a period of evolution.

a. In the early days of accounting, individual postings were made from the previously mentioned sales register to the customers' accounts.

b. As an aid to speed in posting, extra copies of the invoices were prepared. These were sorted in ledger order so as to cut down the time required in finding the ledger account.

c. In more recent years, there has been evolved a "unit method", sometimes referred to as "bookless bookkeeping". Under this method, the copies of the invoices are used as the actual accounts receivable record. This idea was considered revolutionary some years ago, but has now gained wide acceptance. Under such a method, all of the standard accounting controls are maintained:

i. A pre-determined total of sales is secured from the copies of the sales invoices. Summary journal entries establish the accounts receivable control.

ii. In lieu of an actual posting operation, these invoices are filed under the appropriate accounts.

iii. When cash is received, the invoices are extracted and stamped "Paid" with the date. If a partial payment is received, it is either noted upon the invoice to which it applies or a separate slip is prepared and filed with the accounts receivable invoice. In all cases of partial payments, however, a separate slip is prepared for the purpose of proving the "postings" of cash.

d. Cash "postings" are proved with the pre-determined cash receipts by adding the total of the invoices stamped "Paid" to the total of the slips for partial payments, mentioned above.

e. The paid invoices are filed in a separate file at the end of the month.

f. The only operation required at the end of the month is to prepare monthly statements. This can very easily be done with a split platen adding machine which provides for the insertion of the date or the invoice number and the amount. Under such a method, "open item" statements are prepared, that is the customer receives a statement of the unpaid invoices, only. As can be seen, however, a regular statement could be rendered merely by retaining copies of the paid invoices until after the statement was completed.

g. In those cases where the old-fashioned method of posting is retained, it has been found that posting operations are materially speeded by confining the posting operations to two or three periods per month. Under this method, the posting copies of the sales invoices are retained and sorted, and are posted only at periodic intervals throughout the month. The reason for economy is apparent from my previous remarks to the effect that 75% of posting time is consumed in locating, inserting and extracting the ledger sheet.

5. *Methods of Sales Analysis*—The evolution of methods and records for sales analysis was as follows:

a. Originally, the columnar sales register was used.

b. It was then found that a preparation of a sales invoice copy which permitted sorting by hand, materially speeded the analysis problem.

c. Mechanical devices were invented and manufactured to aid this work. The most prominent are the punched card systems made by International Business Machines and Remington Rand, and the mechanical sorting devices known as "Keysort" and "E-Z Sort".

d. In some industries where product analysis is not important, territorial analysis is sometimes desired. One simple method of securing this result is to arrange the accounts receivable cards by territorial filing groups. Thus, the totals of postings to the respective controls automatically provides the territorial analysis.

### Purchases and Accounts Payable

In a discussion of this problem, I have used the term "purchases" to cover both materials and services since the system problem is substantially the same.

*CASH PURCHASES*—Of course, it will be readily understood that expenditures may be made and charged directly from cash on hand or by check. There are many disadvantages of control and efficiency in this method. With respect to cash on hand, imprest funds have been almost universally adopted. This provides the same result as if we treated the Petty Cash Fund as an individual vendor who is paid periodically for the invoices presented by him.

*CREDIT PURCHASES*—Naturally, purchases may be recorded directly from the vendor's invoice as received, but several devices have been introduced for better control.

1. *Evidence of Propriety*—Obviously, it is highly desirable to assure ourselves completely as to the propriety of vendors' invoices before payment. Frequently, this is done by having someone in authority initial the invoices, but this is a very poor device for preventing duplication of invoices since too much reliance is placed upon the memory of the individual approving the invoice. In larger organizations, therefore, the system of internal control has been developed to include purchase orders and receiving tickets.

Two general methods of utilizing these records have been evolved:

a. The receiving ticket and the invoice are sent to the purchasing department which matches up these documents with the vendor's invoice and then initials the invoice for payment by the accounting department.

b. Where the accounting department exercises stronger control over these operations, copies of the purchase orders and receiving tickets are sent directly to the accounting department. In this case, the verification of the authority for purchase, the receipt of the merchandise and the accuracy of the invoice is performed by the accounting department itself.

2. *Form Design*—Without belaboring the subject, similar principles are applied in the design of purchase orders as were previously described under sales analysis.

3. *Methods of Original Recording*—The recording of invoices covering purchases has also gone through an evolution similar to that mentioned under sales invoices.

Here, again, we find the general trend towards the elimination of subsidiary records and the development of the Voucher Register. Under this method, the invoices from one vendor are accumulated for an entire month. These are usually filed in alphabetical order and, at the end of each month, a single jacket known as a "voucher" is prepared for each vendor showing a summary of purchases and an analysis of the accounts to be charged.

Spaces are provided upon the voucher jacket for the recording of the check numbers and amounts in payment or partial payment of the account. Moreover, the voucher register contains provision for the insertion of these check numbers. No posting is made to a vendor's account, but upon payment, the check numbers are inserted in the voucher register opposite the particular voucher and a check mark inserted when the voucher has been completely paid. At the end of the month, a tabulation is made of the vouchers where no check mark appears since these consti-

tute the unpaid vouchers (accounts) payable. Credits for returned merchandise, etc. are handled either by preparing vouchers in red ink, or deducting the amounts from subsequent vouchers. It will be seen, therefore, that under this method, the maintenance of separate accounts payable for each vendor is unnecessary.

### Cash Receipts

Elsewhere, I have discussed the general devices used for internal control. The most modern procedure in the recording of cash receipts consists of the use of "cash dockets". These dockets are nothing more nor less than a notation of the amount received made upon the document accompanying the remittances. This may consist of:

1. A remittance advice from the customer;
2. A duplicate copy of the bill or letterhead returned with the remittance;
3. A detachable stub which is part of the check received;
4. The envelope in which the remittance is received; or
5. A separate slip, created where receipts are not accompanied by any of the above documents.

The use of cash dockets admits of a number of advantages:

1. It permits summary entries to be made in cash receipts books, these being supported by the actual dockets.
2. It permits greater flexibility for speed in posting to accounts receivable and other accounts since several days' cash dockets may be accumulated in the same manner as sales invoices and posted at one time.
3. It provides a very convenient method of control in the segregation of the handling of cash from the accounting for cash.
4. It may be of interest to know that there is at least one adding machine which may be used to create the cash docket and the deposit slip mechanically in one operation. This adding machine has a separate chute which permits the insertion of the document which is to serve as the cash docket. Through the use of a double ribbon, the amount of the cash receipt is imprinted upon the docket and upon the adding machine tape simultaneously. Upon completion of all dockets, a total is struck and this is used as the deposit slip.

### Cash Disbursements

In modern systems, the use of carbon copies of the checks has been almost universally adopted in place of the usual cash disbursement book. This is usually done in conjunction with the use of a voucher register, all entries to expense and asset accounts being made from the purchase vouchers themselves and the only charge from cash disbursements being made to "vouchers payable" except for cash discount. This may be done in either of two ways:

1. Use of ordinary carbon copies of the checks, either individually or in sheets. These, however, yield a somewhat bulky record.
2. Under certain hand and machine methods, checks can be written with the carbonized information contained on one line of a backing sheet, which constitutes the cash disbursements journal and avoids double writing of the information.

For those unfamiliar with the voucher register previously described under purchase routines, it may not be amiss to note that:

1. The checks accompany the vouchers for signature.
2. The check number is then inserted on the face of the voucher.
3. The vouchers are then arranged in numerical order and the check number is inserted in the voucher register by copying it from the face of the voucher.

## General Remarks and Conclusions

Quite obviously, it is impossible to discuss all of the problems associated with system design within the scope of this paper. Special problems such as payroll, with the attendant difficulties of deductions and machine and hand methods used in their preparation, become subjects for individual attention and development. The question of inventory control and detailed cost records would likewise take a considerable amount of time, and the same is true of a host of system problems too numerous to mention.

It has been my purpose in this paper to stress and briefly illustrate that successful systems design must be predicated upon:

1. A thorough grasp of the three essential elements: recording, control, and reporting.

2. The approach should be functional rather than specific.

3. The system designer must approach his problem with an inquiring mind, not fettered by out-worn tradition.

4. Nothing should be inserted into the system which is not *used*.

*Business moves on systems.* The most energetic plans of management will fail unless the proper medium for accomplishment is provided.

# The Certified Public Accountant on the Threshold of his Second Half Century

*By* PRIOR SINCLAIR, C.P.A.

THE members of the accounting profession are gathered here from all states in the Union, from the territories and from other lands in this the fiftieth year since the passage in New York State of the first certified public accountant law.

It is fitting at this occasion that we pause in the consideration of present day problems, review the history of our profession and endeavor to glean from our study of the past, the knowledge that will best serve to guide us in the future.

It is but a few years ago—in 1937—that The American Institute of Accountants celebrated in New York City its fiftieth birthday, for the organization of that national body first known as The American Association of Public Accountants preceded by nine years the passage of the first certified public accountant law.

However, it would be an error to think of the profession in this country as of but 50 or 59 years of age. The early publication of the news of our profession makes many references to informal meetings and round table gatherings of public accountants which took place in the years preceding the organization in 1882 of "The Institute of Accounts" the first National Society of Public Accountants. It was by these group meetings that the need was recognized for a formally established national organization.

It is interesting, and indicative of the pride in being recognized as a public accountant which also then existed, to note that in 1908, in this same city, at a convention of the American Association of Public Accountants, James G. Cannon, an outstanding banker of his day, remarked in the course of his address that he had on his library wall a framed certificate showing his membership in the "Institute of Accounts of New York City."

I have said that the existence of the profession long preceded the formation of its national societies or the passage of C.P.A. legislation. To my mind this is shown by an item appearing in the Journal of Accountancy for October, 1913, reading as follows:

"It is customary to consider the profession of the public accountant as one of very recent date, but apparently there have been public accountants in this country from the late eighteenth century onward.

"Evidence of this is offered by an advertisement which appeared in the *New Jersey Journal* of Wednesday, July 8th, 1795, printed and published by Shepard Kollock at Elizabethtown, N. J.

"The advertisement reads:

"NOTICE

"A conveyancing office and office of intelligence will be opened by the subscriber on Monday next, in the brick house of William Shute, Esq., formerly occupied by Cortland Van Arsdalen; where writings of every kind will be done on moderate terms; also, farmers' and tradesmen's books posted with accuracy and dispatch, and those who do not understand the method of keeping their books will be shown the form.

(Signed) "BENJAMIN THOMSON"

PRIOR SINCLAIR, C.P.A., the President of our Society, is a partner of Lybrand, Ross Bros. & Montgomery. This address was delivered by him on October 3, 1946, at the Fifty-ninth Annual Meeting of the American Institute of Accountants held in Atlantic City, New Jersey.

It seems to me that Benjamin Thomson presented his qualifications in moderate but well chosen words and although the publication of his announcement long preceded the adoption of our Code of Ethics, it nevertheless does it no violence.

As a further indication of the early existence in this country of the professional accountant, the New York City directory of the year 1801—one hundred and forty-five years ago—lists the name of William Connolly, Accountant.

William Connolly was the great-grandfather of one of the present-day leaders of our profession, a man who commands our esteem and affection—my beloved associate—William M. Lybrand.

Our profession owes much to the skill and talent, the broad understanding, the courage and the vigorous integrity of those early leaders of the profession who established the standards of professional conduct which have guided us so well throughout the years and which have contributed so greatly to the advancement of the profession.

Theirs was a difficult task, accounting literature in that day was limited in quantity, but, fortunately, of high quality. In the absence of authoritative interpretations and recognized conventions the public accountants however *had the boldness to follow their reason.* They sought to be not only right but *aggressively right* and the subsequent history of the profession establishes the wisdom of setting such a course.

Let us briefly review the history of the profession in New York State, for the history and growth of the profession in that state parallels that of the nation.

It was on April 17, 1896 that Governor Levi P. Morton, of the State of New York, approved the bill passed by the State Legislature which created the title Certified Public Accountant and defined who should be entitled to be so designated. The first examination under the new law was held in December, 1896. Seventy-five C.P.A. certificates were awarded in that year. It was from this group of certified public accountants that the material came for the formation of the New York State Society of Certified Public Accountants, which was incorporated on January 28, 1897, and which started on its memorable history with eighteen charter members.

The Society was organized on March 30, 1897, at a meeting at the Waldorf-Astoria Hotel, and the first annual meeting of the newly formed society was held on May 10, 1897. At that meeting the secretary reported a total membership of twenty-four, of whom fifteen were in attendance. That the Society was on a sound financial basis with disbursements well within the limit of its revenue was evidenced by the statement of the treasurer reporting receipts of $171.25 and disbursements of $26.00.

The Society promptly entered upon a career of activity; nine meetings were held during the year 1897. It may be that clients' demands were not onerous as I find that in October, 1897, a committee was appointed for the development of a plan of exercise and entertainment for the coming Winter.

The Society was early aware of the need for scholastic training in accountancy subjects training that would bring education in technical subjects to those who desired to undertake the examination for the certified public accountant's degree. It was through the direct efforts of the Society that the New York University School of Commerce, Accounts and Finance was organized and started operation on October 1, 1900.

It is a source of pride that of the fifteen members of the faculty of that school, six were members of the New York State Society of Certified Public Accountants, one of whom, Charles Waldo Haskins, was appointed Dean and who, while already serving the Society as President, nevertheless undertook this additional responsibility.

Thus was formed the first school in this country for instruction in account-

ancy, soon to be followed by others. In comparison, at the present time there are listed in the regulations by the Commissioner of Education of the State of New York ninety-four institutions throughout the country having a course of study of a satisfactory standard to meet the present requirements of the Certified Public Accountancy Law of New York State.

Thus a few farsighted men in those early days started the schools and universities of this country on the pathway of accountancy instruction and in the following years as the demands of the public for the services of public accountants grew, trained men, skillful and in ever-increasing numbers were available to meet that demand.

It would be most propitious if time on this occasion permitted a reference to each of the many members who in those days devoted themselves unstintingly to the affairs of our societies and by so doing contributed so greatly to the advancement of our profession. It would be amiss entirely to omit such references, as societies consist of members; the character and quality of the group does but reflect those of the individuals. Our Society quickly demonstrated its quality, its members *had* quality.

Mention has been made of Charles Waldo Haskins who served the New York State Society as President from its inception in 1897 until his death in 1903. Serving as officers or directors in those early years you will find listed Arthur W. Teele, our first Secretary, Farquhar J. MacRae a charter member serving first as a director and later as President. Farquhar J. Mac Rae is the only living charter member of the New York State Society and during the past year the New York State Society of Certified Public Accountants presented him with a special Charter Member Certificate commemorative of fifty years of loyal membership in the New York State Society of Certified Public Accountants.

Among others prominent in the New York State Society's affairs in those years were F. W. Lafrentz, John R. Loomis, Elijah W. Sells, John B. Niven, Samuel D. Patterson, who later served as Secretary for many years, Edward L. Suffern, Charles E. Sprague, under whom I studied, and Sanders W. Davies, later the first President of the American Institute of Accountants. The limitation of time does not permit the mention of others also worthy of your admiration.

Those were busy years; matters under consideration were of extreme importance; the decisions made set the pattern for the future. During the first ten years of the Society's existence there were five attempts by others to secure legislation amending the New York C.P.A. law. The Society was diligent and succeeded in resisting the attempts to lower the standards of eligibility. In subsequent years, changes in legislation have provided for the changes in public need.

In those same years, practitioners in other parts of the country were also active, forming in groups, tackling the problem of appropriate State legislation and striving to perfect the national organization, The American Association of Public Accountants, which in 1887 the public accountants of Pennsylvania were largely instrumental in bringing into being.

Pennsylvania was the second state in the union to benefit by C.P.A. legislation. Pennsylvania was fortunate in having such sterling leaders as John W. Francis, John Heins, Charles N. Vollum, Joseph E. Sterret, William M. Lybrand, T. Edward Ross, and his brother Adam A. Ross, the then and now youthful Robert H. Montgomery, and Geo. Wilkinson of Illinois, then a nonresident member of the Pennsylvania Institute of Certified Public Accountants.

In the efforts to bring about a national organization and to build a firm foundation for our profession we were fortunate in also having the warm, enthusiastic and able assistance of our

brethren from overseas. The wise counsel of Mr. Edwin Guthrie helped greatly in the early task of organization. Arthur Lowes Dickinson contributed generously from his fund of understanding and experience. The aid these men rendered in solving early problems of the profession is beyond measure.

In the ensuing years professional activities moved forward with greater rapidity. Public recognition grew, and our responsibilities increased. With the growing public recognition and the expansion of the nation's commerce and finance, practitioners grew in numbers and experience.

With the advent of federal income tax legislation taxpayers looked to public accountants for assistance. The determination of the amount of taxable income and the amount of tax thereon requires keen accounting skill and understanding. So serious is the impact of taxes, that businessmen must know before entering into a transaction its possible tax effects. Accountants' views on tax legislation were sought by Treasury advisers, legislative committees and the administrators of the law. Income tax laws today are intricate ofttimes obscure—our recommendations have been consistently directed toward simplicity. I wonder if taxpayers realize how much worse the laws would have been if we had not made suggestions for improvement.

A bulletin entitled "Approved Methods for the Preparation of Balance Sheet Statements" prepared by a committee of the American Institute of Accountants and released in 1917 by the Federal Trade Commission and approved by the Federal Reserve Board served to inform the public, particularly lenders and credit grantors, of the character and scope of the public accountants' work. Throughout the years revisions were made and the latest issue, including revisions to 1936, entitled "Examination of Financial Statements by Independent Public Accountants," is still authoritative.

The establishment by the American Institute of Accountants of research committees and the issuance of Bulletins presenting their viewpoints on auditing and accounting matters serve to keep the entire profession informed on vexing questions as they arise. This work is now ably supported by an executive of the Institute, the Research Director, and a staff of assistants.

The growth in published material available for the benefit of the membership is impressive. In 1910 the New York State Society in its yearbook, catalogued 126 volumes available in the Society's library—today the library of the Institute contains 25,000 books and pamphlets, many written by its members.

In November, 1905, 41 years ago, the first number of The Journal of Accountancy was published under the auspices of The American Association of Public Accountants, the forerunner of the present American Institute of Accountants. It was under the able editorship of Joseph French Johnson, Dean of the New York University School of Commerce, Accounts and Finance and Dr. Edward Sherwood Meade, Director of the Evening School of Accounts and Finance, University of Pennsylvania.

The first number of the Journal contained articles entitled:

"Education and Training of a Certified Public Accountant"—By J. E. Sterrett, C.P.A.

"Duties and Responsibilities of the Public Accountant with regard to New Issues of Stocks and Bonds" —By Arthur Lowes Dickenson, M.A., F.C.A., C.P.A.

"Professional Standards"—By Robert H. Montgomery, C.P.A.

"The Scope of the Profession of Accounting"—By F. A. Cleveland, Ph.D.

The articles by their titles evidence the keen sense of public responsibility that even at that early date constituted the

fibre of our professional body. It continues to be our main strength.

The worth of these contributions to the first number of the Journal stands today unimpaired by the passage of time. A periodic rereading of these articles would serve to strengthen us for the problems of our times.

The Journal of Accountancy has been and continues to be outstanding in the field of periodic accountancy literature.

Notable gatherings of the profession took place throughout the years, events, each worthy of complete description. The International Congress of Accountants was held in St. Louis in 1904. Many friendships grew out of that meeting; it was the first meeting of our young profession which had the added flavor of distinguished representation from other countries. The memory of it still warms the hearts of those fortunate in having attended. Annual conventions were regularly held but war came and interrupted the international gatherings. The next meeting of international character was held in Amsterdam, Holland, in 1926. This, I believe, was the first meeting abroad attended by delegates from this country. The friendly feelings engendered by these international conferences resulted in more frequent like gatherings and the meeting at Amsterdam was quickly followed by a meeting in New York in 1929 and in London in 1933. The fiftieth anniversary meeting of the American Institute of Accountants was held in New York in 1937, and while not international in title, it was decidedly international in character and attendance. Again war intervened. We are happy to see here today our professional brethren from other lands and hope the day will soon arrive when we can again gather together from all parts of the world, benefit by the exchange of ideas and enjoy the companionship of our fellow practitioners from the world over.

These conventions or gatherings have been of inestimable benefit to the profession. Not only have they brought to us the finest accounting thinking as exemplified in the technical papers presented at these meetings and later printed and preserved as part of our accounting literature, but, of perhaps equal importance, they have led to the forming of friendship of lasting character and have opened our eyes to the fact that fellow practitioners here and abroad are really delightful fellows and have in them those qualities we most respect and admire.

An important contribution to the development of these friendships and understanding took place when the thoughtfulness and generosity of Elijah W. Sells made possible the founding of the "Accountants Club." Let us hope for the return of conditions which will permit of re-establishing that friendly gathering place.

These friendships have been not only a source of satisfaction and enjoyment but have served us well in the past and should be preserved as they will also serve in the future. It was our faith in the sincerity and honesty of members of both organizations that made possible in 1936 the merger of the two national organizations into the one in which we enjoy fellowship today. The work of Durand W. Springer in gathering together certified public accountants from throughout the country into the American Society of Certified Public Accountants served the profession well, and his appreciation of the desirability of one national organization helped tremendously in accomplishing that objective.

My remarks have been sketchy and fragmentary. They do not constitute a history—even in skeleton form. But we have a history, a history of which to be proud; it should be brought together and preserved—it is well worth preserving. Its study would inspire and enlighten us and those who follow. In this connection I bring to your attention a report by the "Committee on History" in May of this year to the Council of the American Institute, containing the following recommendation:

"Your committee is of the opinion

that as soon as feasible it would be advisable for the Institute to employ some one to supervise the compilation of the historical material now on hand and which may become available later. The cooperation of the American Accounting Association, no doubt, could be secured in furthering this work. It might be possible also, for students in some of the colleges and universities to do research work with the encouragement and assistance of accountants, especially in states in which little has been accomplished heretofore in the assembling of historical data."

It is my belief that we all heartily endorse that recommendation.

Over the years no great changes have occurred in fundamental accounting and auditing concepts; great progress has been made in the technique of their application and presentation. It was, is and will be the purpose of Certified Public Accountants to speak the truth and we must resist to the fullest any attempt from whatever source which seeks to curb our right to so speak.

The Securities and Exchange Commission and other governmental bodies entrusted with the administration of regulatory laws likewise but seek the truth. Ofttimes truth is elusive. Honest differences arise as to what constitutes truth. We may differ as to the form or manner of its presentation. We may differ as to the adequacy of its presentation. But let us concentrate on the solution of those problems and not hinder our progress by devoting our efforts to the undue refinement of unessentials.

In seeking in the past guidance for the future I can do no better than to quote to you from an address by the President of the Institute at the annual meeting and fiftieth anniversary celebration of The American Institute of Accountants, held in New York in October, 1937. I quote:

"We shall retain our strength just as long as we retain our independence—no longer.

"If anyone outside of the profession—governmental or private, client or friend—is stronger than we are and is able to tell us what to do, is able to influence a statement or a report against our best judgment, from that moment the profession will deteriorate. It is not so today."

and we can add with today's dating,

It is not so today.

As long as by our character and by the application of skill and talent to the tasks entrusted to us we demonstrate that the profession rightly serves the public interest, our reputation will remain secure.

Today the New York State Society stands 5,100 strong—in complete harmony with our fellow accountants—ready and willing to contribute to the full of our capacity in collaboration with the American Institute of Accountants and its 11,000 members, in the furtherance of the nationwide interests of the profession.

In conclusion—let me direct your attention to a pamphlet published in 1942 entitled "Pioneers of Organized Public Accountancy in Pennsylvania." It was written by one of the founders of the Pennsylvania Association of Public Accountants, later organized into the Pennsylvania Institute of Certified Public Accountants. There appears on the title page of that pamphlet a quotation taken from an inscription on the Archives Building in Washington, D. C., which states:

"The heritage of the past is the seed that brings forth the harvest of the future."

We have a precious heritage. Let us nurture it carefully.

# College Education as a Requirement for Certified Public Accountants—The New York Experience

By Norman E. Webster, C.P.A.

This is the second occasion when I have been honored with an invitation to appear upon the platform of this Association. The other was at the Atlantic City meeting in December, 1937. That was less than one week before the effective date of section 1498-a of the New York CPA Law of 1929. By reference to *The Accounting Review* I find that the subject of my paper was "*Higher Education for Public Accountants.*" For this meeting I am asked to write upon the subject, "*College Education as a Requirement for Certified Public Accountants—The New York Experience.*"

Inasmuch as both subjects relate to education for accountants, it may be appropriate for me to detail to you all my qualifications for these assignments even though modesty might suggest that I leave that to others. But modesty is not my outstanding characteristic.

During all 16 weeks of the fall term in a small town school in Michigan when I was 12 years old, I studied a book by Ira Mayhew, A.M.,—*A Practical System of Bookkeeping,* which was first published in 1851. That recital covers all of my formal schooling in this subject and with it you will better understand the weight you should give to what follows.

If with this paper I put you to sleep or empty your chairs that will not be with a mass of statistics, even though it is with figures that an accountant does a large part of his work. However statistics related to this subject have been compiled and presented in two documents and as I shall refer to them perhaps I should mention them now. They are: "*The Administration of the CPA Law in New York State*", by Harlan H. Horner, Assistant Commissioner for Higher Education in New York State, which was printed in *The New York Certified Public Account* of January, 1935, Vol. 5, pages 32-56; "*Analysis of Candidates Admitted to the CPA Examinations since Jan. 1, 1938*" by Eckes & Dean, CPA's., in Report of May 15, 1944, 10 pages 13" x 19" and 10 pages 13" x 14".

Both authors were well prepared to make these studies. Dr. Horner came to New York in 1904 with the new Commissioner of Education, Dr. Andrew S. Draper, president of the University of Illinois, where an interest in education for business and accountancy was further promoted by its next president Edmund J. James. And during most of his service in New York Dr. Horner had been in charge of or closely asociated with the matters of edu-

Norman E. Webster, C.P.A., has been a member of the Society since 1911, and is a partner of the firm of Webster, Horne & Elsdon of New York. Mr. Webster has been a member of the Board of Certified Public Accountant Examiners of New York State since 1930, and Chairman of the Board since 1934. He has been in public practice in New York since 1909.

This paper was read by Mr. Webster at the meeting of the American Accounting Association held in Chicago, Illinois, on September 6, 1946.

cation and examinations for all the professions. And Walter N. Dean, BCS at New York University School of Commerce in 1910, CPA 415 of New York in 1913, in public practice as a principal during over 30 years, and for a time a teacher at St. John's University School of Commerce, has been Secretary of the New York Board of CPA Examiners since July, 1930, and more recently Secretary and now President of the Association of Certified Public Accountant Examiners, in which the Examiners of all States and the American Institute hold membership.

The first of these studies was prepared for an address before the State Society and covered 75 examinations from December 15, 1896, to October 1, 1934, with a more detailed study of the 10 examinations during the last 5 years of that period. The second study was made at the request of the State Education Department and paid for by the State Society. It brought down to June 30, 1943, the statistics in the earlier study; and for the 5 years from January, 1938, to April, 1943, it presented an analysis of the education and examination results of 2011 out of the 3302 Candidates who were admitted to the examinations during that period.

As to the Candidates analyzed or omitted the Report stated: "The number analyzed covered 90% of the Candidates admitted prior to October 1941 and, for the most part, the ones not included in the analysis could have taken no more than one, two or three examinations. In all probability, the inclusion of 1300 more candidates would not materially change the percentages shown in these exhibits, and with the prevailing uncertainties of war and Selective Service in 1942 and 1943 the earlier years reflect more normal conditions."

Perhaps this is a good place to note that the Report shows that during the 47 years from April 17, 1896, to June 30, 1943, the New York State Board of CPA Examiners rated the answer papers of 53,142 Candidates—which number of course includes the several trials of many Candidates. The failures totaled 42,839 or 80.6%, and of the 10,303 Candidates who were passed or 19.4%, certificates were then issued to 9,324 Candidates who had the required experience. Quite likely you know that New York examines about one-third of all the Candidates in the United States.

Besides the 9,324 certificates issued upon examination to June 30, 1943, 183 certificates were issued during the first few years under the waiver provision of the original Law, and after July, 1918, 655 certificates of other States were indorsed by New York. No doubt you all know that such indorsement is not limited to reciprocal action by the other States. New York does not require reciprocity for its indorsement. After 3 years of the public practice of accountancy in any State or States, either as principal or staff accountant, and with residence or place for the regular transaction of business in New York State, New York will indorse the certificate of any State whose requirements at the date of the issuance of its certificate were equal to those of New York at the same date.

The subject assigned to me included The New York Experience which, of course, referred to the College Education as a Requirement for Certified Public Acountants. What I can tell you as to the experience of the Candidates must necessarily be almost wholly objective. And for that perhaps it may be instructive to consider the Candidates' results in examinations both before and after the introduction of the requirement of completion of the 4-year course in a college or school of accountancy. You know of course that the New York Law does not require a degree. While such courses of study in most institutions lead to degrees, some do not. Perhaps degrees mean more to educators than to accountants

who almost never mention their degrees except in connection with their technical authorship, and some omit them even in those cases.

In my 1937 paper I presented some statistics from the study by Dr. Horner of the 5 years 1929-1934 which showed that, of 7,371 Candidates, 604, 8.2% college trained men and 6,767, 91.8% high school, out of each group in a single examination—not always their first—4% passed all 4 subjects, 14% passed 3 subjects, and 12% passed 2 subjects—making 30% of each group who received some credit, while 26% of the college men and 28% of the others passed only one subject. But Mr. Dean's analysis of the 5 years 1938-1942 showed that of 2,011 Candidates, all college graduates, in their first examination 320 (15.9%) passed all 4 subjects, 323 (16.1%) passed 3 subjects, and 646 (32.2%) passed 2 subjects, making nearly 62.2% who received some credit. This suggests that the college graduates in the 1938-1942 examinations were much better prepared than the college men in the 1929-1934 examinations. However the results during these two 5-year periods would not be fully comparable if there was a marked difference in the difficulty of the examination questions or in the severity of the ratings in the two periods. Perhaps that may not be of importance because after May, 1930, there were only 2 changes in the personnel of the New York Board of CPA Examiners.

Before leaving this discussion of the experience of Candidates under the College Education Requirement, I shall insert here some statistics as to the examination results of 700 Candidates admitted during the year 1934, and a comparison with the similar results of the 2,011 Candidates admitted during the 5 years 1938-1942, whose records were analyzed in the Dean report.

| | **700 Candidates Admitted 1934** | | | **2,011 Candidates Admitted 1938/42** | | |
|---|---|---|---|---|---|---|
| Exam. No. | Persons Taking | Passed 4 Subjects | Dropped Out | Persons Sitting | Passed 4 Subjects | Dropped Out |
| 1 | 700 | 29 | 232 | 2.011 | 320 | 337 |
| 2 | 439 | 46 | 217 | 1,354 | 341 | 264 |
| 3 | 176 | 31 | 93 | 749 | 200 | 141 |
| 4 | 52 | 19 | 32 | 408 | 128 | 85 |
| 5 | 1 | — | — | 195 | 77 | 29 |
| 6 | 1 | 1 | — | 89 | 31 | 19 |
| 7 | — | — | — | 39 | 18 | 10 |
| 8 | — | — | — | 11 | 4 | 3 |
| 9 | — | — | — | 4 | 4 | — |
| Attempts | 1,369 | | | 4.860 | | |
| Persons | 700 | 126 | 574 | 2,011 | 1,123 | 888 |
| % | | 18.0 | 82.0 | | 55.8 | 44.2 |

If the 6 examinations taken by the 700 Candidates admitted in 1934 and the 10 examinations taken by the 2,011 Candidates admitted during 1938-1942 were fairly comparable as to difficulty, and if the ratings given to their answer papers were correspondingly fair (I say "if" because I participated in the preparation of the questions and in the individual and collective consideration of the ratings thereon) then the 1938-1942 Candidates had better staying power, because 195 or 9.7% remained after 4 examinations—of whom 134 finally passed on their 5th to 9th attempt, while only 1 of the 1934 Candidates kept on after his 4th examination. However this is not a comparison of college men only, because the 700 Candidates in 1934 included a large number, probably much over one half, who had not gone beyond high school. But for a consideration of the results of their education perhaps only the first or first two examinations should be taken because a large proportion of

those who failed at first prepared for further attempts in coaching courses or by self instruction.

Turning to the experience of the Examiners I am somewhat better informed. For the 100 examinations during the 50 years 1896 to 1945, the New York State Board of CPA Examiners prepared its own questions. This is true although for the last 3 the questions in Commercial Law were the same as those in the uniform CPA Examinations, prepared by the Board of Examiners of the American Institute for the States which used its service. The use of the same questions in that one subject resulted from the fact that having that subject for the New York Board and being of the two members of the Institute Board that prepared the Law questions for the Uniform Examination I economized in time and effort by using questions with which I was satisfied for both examinations.

In passing let me call your attention to the fact that the American Institute of Accountants does not give examinations and has not done so for about 10 years. There is no Institute examination even though that expression is heard too frequently. In confirmation of this statement I refer you to the editorial on page 91 of the February, 1946, issue of the Journal of Accountancy. And even though for 1946 at least, New York will use the questions of the Uniform Examination it will still be one for which our Board assumes responsibility.

As to the severity of the examinations, in New York State the New York Board has considered that it should be set for the level of semi-seniors although the Institute Board at least for a time felt that it should be set for senior accountants. And as to the reasonableness of the ratings the practice of the New York Board has been that the original or tentative ratings should be rather strict or severe, so that when the Board met to compare ratings on the 5 papers in 4 subjects it might consider good marks in one or more subjects as a basis for raising to the passing mark of 75 the rating on some subject so as to give a Candidate as much credit as possible. And when a Candidate requests a review of his rating in some subject (formerly allowable on ratings of 60, but not only on 65) the Board considers his ratings in that subject in all prior examinations.

As to the Candidates' educational preparation for the examinations, I would think that the results in their first examination would be a fair measure of the quality and quantity of the instruction which they had received—if, but only if all other conditions were equal which, of course, they were not and could not be. The 2,011 Candidates admitted from January 1, 1938, to April 1, 1943, came from 55 schools of which 27 schools furnished only 34 Candidates. Of the other 1,977 Candidates, 1,797 came from 13 schools in New York State, 693 to 4 each; and 180 came from 15 schools in other States, 47 to 4 each. Many of these 180 had been suggested to and interviewed and engaged by representatives of New York firms. Probably they were from the groups of high ranking students in their schools. On the other hand the 1,797 from 13 New York State schools probably were from all ranks in those schools, top, middle and bottom. If these surmises were correct, I expected that the Candidates from other States would show better in their first examinations than those from New York State schools.

That proved to be the fact. Of the 1,797 Candidates from 13 New York schools 277, 15.4%, passed their first examination and of the 180 from schools in other States 38, 21.1%, passed. But individual schools did not conform to that pattern. They showed some striking variations. The highest result, 50%, was from another State school with 2 passed of 4. The next highest, 37.5%, was shared by one other State, with 3 passed of 8, and by one New York school with 10 times the

Candidates, with 30 passed of 80. The next 3 groups were 1st, one other State school 33.3%, with 2 passed of 6; 2d, two other State schools each with 2 passed of 8 and one other State and one New York State school each with 1 passed of 4, 25% in each of 4 schools; and 3rd, one other State school with second largest list, 23.5%, for 8 passed of 34. But the next highest, 22.2%, was a surprise to me because it was the New York school with the largest group of Candidates with 154 passed of 693. Then the next highest, 21.3%, was one other State school with 10 passed of 47. The percentages of 10 other New York Schools and of 7 schools in other States ranged from 20% down to none from one New York and one other State schools who had only 4 and 6 Candidates in the examination.

This study of the examination results of 180 Candidates from 15 schools in other States and of 10 times as many from New York State schools convinces me that students who have spent 4 years in the day classes or 6 years in the evening classes in the schools have been exposed to a quantity and quality of instruction which should have prepared them for the examinations in Commercial Law, Theory of Accounts and in the theoretical parts of Auditing. I never have believed that schools were or could be prepared to teach successfully the subject of Practical Accounting or the practical part of Auditing.

Recent developments have only strengthened this opinion. During many years when Candidates in New York were permitted to take all 4 subjects when they had the educational requirement and one year of experience in simple accounting or bookkeeping, the failures in Practical Accounting far outnumbered those in any of the other 3 subjects. A few years ago the New York rules were revised to require that before a Candidate would be admitted to the examination in Practical Accounting, he must have had besides the other qualifications two years experience in public practice in the employ of a CPA. This change did not affect the other 3 subjects. The result has been that the failures in this subject have been reduced and now are much fewer than those in Auditing. I expect that in the future Auditing will be divided into its Theory and its Practice, and that CPA experience will be required before a Candidate is admitted to sit for Auditing Practice.

I do not wish to belittle the efforts of the schools in their attempts to teach Practical Accounting and Practical Auditing by means of laboratory work. But the situations and transactions which they are able to put before their students in the laboratories are those which have arisen in CPA offices years before, whereas many such offices are confronted with novel situations at least once a year and usually much more often. Without denying the importance of school work for the beginner, experience in practice is even more essential.

As I have indicated I believe that the experience of the New York State Board of CPA Examiners has demonstrated the value of College Education as a Requirement for Certified Public Accountants. Instead of 50-50 apportionment between liberal arts and technical subjects I would have preferred 60-40 or even 75-25. If accountancy is a trade only, we should cut out the cultural subjects to save time. But if it is a profession, then practitioners should be educated men. However, since New York has started out with the 50-50 apportionment of a 4-year course, I do not advocate a change in that proportion for the present. But when the courses are to be lengthened I hope that the change will be by the addition of at first one year, later two years, to the fundamentals, English, History, Science, perhaps Languages.

Thus far I believe I have not criticized the schools. But I can and shall. In so far as I know they are using good

tools and wise methods. However, it must be that their inspection of the materials on which they work is lax or non-existent. Manufacturers do not accept their vendors' assurances of the quality of the raw materials they purchase without inspection and tests of the materials. If any should do so the buying public would soon be rejecting the manufacturers' products just as the CPA Examiners are rejecting too large a proportion of the product of the colleges and schools of accountancy.

A high school diploma does not insure that the holder has satisfactorily completed a 4-year course in that school. The New York State Board could give you many illustrations but I have time only for citation from two letters from one college graduate. Both letters contained a word spelled *p-r-i-v-a-l-a-g-e*. One also had these spellings *s-u-f-f-i-e-n-t* and *g-r-a-t-i-o-u-s-l-y*. And one had *e-x-p-e-d-i-a-t-e* while the other simplified it to *e-x-p-i-d-i-t-e*. Bad grammar, big words where they do not belong, inability to read or understand what they read. Unless the schools will do the necessary screening, the Examiners must continue to do so.

# College Education as a Requirement for Certified Public Accountants in New York State

## (From the Viewpoint of the Practitioner)

*By* Raymond G. Ankers, C.P.A.

The New York State C.P.A. law specifies that candidates for the examination leading to certification must be graduates of colleges or schools of accountancy registered by the State Education Department as maintaining satisfactory standards. To meet satisfactory standards, a school must offer a four year course or its equivalent in cultural and business subjects including 24 hours of accounting, 8 hours each of business law and finance and 6 hours of economics. You will observe that a candidate need not have a college degree to take the C.P.A. examination and conversely, the fact that a candidate holds a degree does not necessarily mean that he possesses the necessary background to take the examination. However, an education at college level and consequently most candidates are with a major in accounting is required college graduates.

Raymond G. Ankers, C.P.A., is the personnel manager of Lybrand, Ross Bros. & Montgomery, C.P.A.'s, New York. He is a frequent author of articles on the subject of staff selection and training, and is a member of the Advisory Board on Occupational Guidance and Placement of Pace Institute. Mr. Ankers is a member of the Society's Committees on Education, Membership, and Publications. He is also a member of the American Institute of Accountants and of their Committee on Education.

This paper was read by him before the 1946 annual meeting of the American Accounting Association recently held in Chicago, Illinois.

The New York State C.P.A. law setting these minimum scholastic requirements did not become effective until January 1, 1938, but it should be noted that the legislation putting it on the books was enacted several years earlier. Because of the broad implications of this law, the effect of its enactment was not limited to New York State. Without question, it had a profound effect upon the employment policies and practices of public accounting firms throughout the country. It also set a criterion for an accounting major which many schools throughout the country considered expedient to follow.

I do not mean to infer that prior to the enactment of this legislation, public accounting firms did not favor college graduates when employing men for their staffs—because as a matter of fact they did. For many years it had been the practice of a number of firms to employ college graduates almost exclusively. However, before the passage of the New York State law, there was less uniformity in the scholastic background of men employed by public accounting firms. For example, some graduates had majored in accounting but others had little, if any, technical training to fit them for the public accounting field. Why did public accountants employ men having such diversified backgrounds? They had little choice. They knew they needed well educated men but found only a limited supply of high grade accounting majors who intended to make public accounting a career. The supply was far short of the demand.

However, after the enactment of the New York State C.P.A. law the supply of accounting majors indicating interest in public accounting increased. It seems as though the college education requirement as a prerequisite to becoming a C.P.A. gave public accounting more prestige in the minds of students and made them more conscious of the opportunities existing in this field of endeavor.

The law was of assistance to employing practitioners in another way. It provided a yardstick by which they could gauge the adequacy of the technical training of applicants. As you know, most public accountants are not educators — therefore they probably had some difficulty in evaluating the scholastic records presented to them by applicants. Subsequent to the enactment of the law, employers could refer to the list of schools registered by New York State to determine whether the applicant had met certain minimum requirements.

Why do public accounting firms consider college graduates with an accounting major as best qualified to enter the public accounting field? To answer this question, let us review the experience practitioners had in training graduates who lacked accounting knowledge. In the first place, as a condition of employment these graduates agreed to study accounting and related subjects at night schools or by correspondence. Then, after a short indoctrination period in the office of their employer these beginners were assigned to accounting engagements. Obviously, for many months they were used only on routine work requiring little or no accounting knowledge. Furthermore, their work was performed under close supervision. Later, as they gained technical knowledge and skill, they were gradually given more responsibility. Their progress was slow for several years but today many of these men hold high positions both in public accounting and in the business world.

For the most part, practitioners were satisfied with the results obtained in developing these beginners. However, there were two important reasons why they did not wish to continue this practice. First, men without necessary technical knowledge took too long to develop. For example, college graduates with little or no training in accounting and related subjects required approximately four years to progress to the rank of semi-senior accountant whereas graduates who had majored in accounting advanced to the same rank in about one-half that time. The other reason is that public accounting firms were and still are reluctant to send beginners without accounting knowledge to clients' offices even to perform the most routine work.

What I have said about college graduates with accounting majors as being the most desirable applicants because of their technical background raises another question. Why are not men who have had specialized training in accounting and related subjects, but lack a complete college education considered adequate? Surely men with good accounting training can be sent to clients' offices in the capacity of junior assistants, make a creditable showing and cause their employers no embarrassment. Although this may be true, to progressive employers it is not enough. Employers set their sights on the future—they want to take all steps possible to satisfy themselves that today's beginners have those qualities necessary to become top seniors, supervisors or members of their firms. Having this point of view, employers look for men with a liberal education in addition to an accounting specialization. The kind of men they seek should possess keener perception, better judgment and a sounder understanding of human relationships than men trained along narrower lines.

I do not mean to intimate that a liberal college education is an open-sesame to these characteristics, nor do I mean to infer that men without benefit of this liberal education could not

acquire these characteristics. There are a number of men at the top of our profession today who do not possess a college degree but, in most cases, these are men who have grown with the profession or who are exceptional and probably would obtain a high position in whatever field of endeavor they attempted.

Now let us move to another question. Are employers satisfied with the training received by graduates of those schools throughout the country which meet the New York State educational requirement? The answer to this question is a qualified "yes." I believe that employers are very well pleased with the accounting knowledge and general background obtained by these graduates. However, most practitioners find them to be inadequately prepared in auditing and woefully deficient in the use of English, both oral and written.

These weaknesses have been discussed at some length at the last two joint meetings of the Committees on Education of the American Institute of Accountants and of the American Accounting Association. This subject has also had the serious consideration of the Committee on Education of the New York State Society of Certified Public Accountants. It appears to be the consensus of those with whom I have talked that the weakness in auditing is the result of insufficient time spent on instruction of auditing fundamentals and, probably in some instances, a lack of practical knowledge on the part of instructors in the application of auditing principles. It seems doubtful that adequate auditing instruction can be given in the usual four hours allotted to this subject.

The deficiency in the use of English is not primarily the responsibility of colleges. Colleges, it would seem, are responsible only because they enroll students who are so deficient in the use of English that the deficiency cannot be overcome within a period of four years. I understand that some colleges are stiffening their entrance requirements in an endavor to correct this condition. It is possible that colleges could do more in cultivating the proper use of English, both written and oral, if the subject were treated as important in every class as it is in English c'asses.

Earlier in my talk I mentioned that before the passage of the New York State C.P.A. law there was only a limited supply of high-grade accounting majors who were interested in public accounting as a career. Within the next few years I believe there will be a complete reversal of this condition. The change will be brought about by the relatively large number of war veterans who are apparently interested in public accounting.

As nearly as I have been able to determine, many veterans chose this vocation while still in military service because of one or more of the following reasons:

(1) The itinerant nature of the work appealed to them.

(2) They were impressed by the evident need for accountants during the war and the consequent opportunities open to service men having accounting knowledge to obtain commissions or "soft" jobs.

(3) The result of so-called aptitude tests and advice of so-called vocational experts.

(4) They held minor positions as bookkeepers and clerks before the war. Now they want to better their positions. The G. I. Bill gives them the opportunity to study accounting at government expense.

I fear that many veterans have been ill-advised in choosing the public accounting field and that others will fall by the way-side when they learn that public accounting is not a "soft" job. But, there will be many who are peculiarly well fitted for public accounting. I sincerely hope that the vocational guidance departments of colleges will carefully screen veterans to determine

their qualifications and I also hope that those who do the screening will not select introverts as being fitted for public accounting work.

In talking with veterans, I find that most of them know they will require a college education to succeed in public accounting. Of course, most of the veterans I talk with are from New York State and accordingly they would expect to meet the requirements of the C.P.A. law of their home state. However, the unusually large enrollments in accounting departments of colleges indicate a general acceptance of a college education as a prerequisite to entering the public accounting field. With the acceptance of the need for this educational background by so many practitioners and by young people who plan to enter the profession, is it not surprising that only New York State has a four year college level educational requirement?

Probably we should not be too surprised. The accounting profession in this country is only 50 years old and I believe it can be justifiably proud of the progress it has made during this relatively short period. Furthermore, the teaching profession is entitled to share in the credit for this progress. Certainly without the continued cooperation and energetic effort on the part of members of accounting departments of colleges and schools of business administration this rapid progress could not have been made.

The New York State C.P.A. law with its present educational requirement, has been effective for only ten years. In this short time it has been a potent influence in increasing the prestige of the profession and in elevating the educational level of practicing accountants—not only in New York State but in all the states.

## The Briefcase

For professional men only, a briefcase is almost a limb. Briefcases have played a great part in my own life; I know how dear they can be. The briefcase is the professional man's breviary, his bourse, his book of common prayer. If you knew all about briefcases, you'd have the secret of many things.

From—*"The Consolable Widow"*
*By* CHRISTOPHER MORLEY
In Ellery Queen's Mystery Magazine

# Taxpert's Thanksgiving

*By* Lewis Gluick, C.P.A.

I am thankful for Section 23 (x) of the Internal Revenue Code, which permits me to deduct extraordinary medical expenses for 1946; and pray I won't have to avail myself of it for future years.

I am thankful for the New York State Society's Insurance plan; and I pray I may always pay my premiums promptly and never need to collect benefits.

I am thankful I can get some butter, despite the price; but pray Congress will see the cruelty and folly of maintaining the margarine taxes. (I.R.C., Sec. 2301)

I am thankful for my terminal leave pay and its exemption from tax; and pray that Congress will realize that *all* service pay and pensions should be exempt.

I am thankful to the California College of Commerce for giving me the pleasure of teaching my profession as well as practicing it; and pray that I may merit my fee by educating a future generation of good auditors and taxperts.

I am thankful for the many readers who have expressed their appreciation for my short contributions in 1946; and pray for guidance to write as well in 1947, so I may continue to enjoy their patronage.

## COMMITTEE ACTIVITIES

**Question:** May I respectfully ask for an opinion as to the propriety of the professional conduct of those accountants who operate private accounting (CPA) course schools and who employ newspaper and other advertising media? Does such advertising come within the bounds of proper professional conduct?

**Answer:** Your recent letter to the New York State Society of Certified Public Accountants has been referred to the Committee on Professional Conduct. It is the opinion of the Committee that a member of the Society who is identified with accounting course schools may include his name and the initials "C.P.A." in any advertising matter issued by such schools providing the advertisements are dignified in character and contain no misrepresentations or misleading information. It is believed by the Committee that a member should not make any reference in such advertising material to any public accounting practice with which he may be identified.

—Committee on Professional Conduct
Harold B. Simpson, *Chairman*

# PROFESSIONAL COMMENT

*By* EMANUEL SAXE, C.P.A.

## Some Thoughts on Education for Public Accountancy

When Congress enacted the G. I. Bill of Rights, probably none of the members then envisaged the tremendous impetus to higher education which was provided by this law. A study recently made by Dean Partsch of Rutgers University indicates that by 1950, an estimated 6,000,000 students will have been enrolled for study at the college or university level.[1] Although this phenomenal enrollment is expected to recede to about 3,733,000 by 1960, nevertheless, that will still be twice as many students as were attending in 1940.

Recent indications disclose a rather considerable surge towards enrollment in education for business, with a substantial proportion of these students planning to major in accounting.[2] Nor did this trend in higher education toward preparation for an occupation or profession escape previous notice.

Thus, a nation-wide survey among 4,000 students in 41 colleges, conducted by the American College Publicity Association, indicated a 90% vote for a college course which would combine the teaching of how to live and how to make a living.[3] Benjamin Fine reported that in Minnesota, 2,500 freshmen said they wanted a good education to prepare them for leisure-time activities and for citizenship, but that they also equally wanted training for a job.[4]

In March of 1945, the American Council on Education reported on a study of the future educational plans of overseas fighting veterans, which was conducted by 14 officers in charge of education work for the Armed Forces. The consensus was that the men in uniform looked forward to the type of education that would prepare them for jobs.[5]

Shortly thereafter, the Fortune survey conducted in collaboration with the Committee on Post-War Training at Yale University, reported an almost unanimous desire for the importance of vocational training: 87% of the adult civilians polled in this survey felt that training to fit a person for a specific occupation or profession was an important purpose of college education for the individual concerned.[6]

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1 *The New York Sun* (Editorial), August 2, 1946.

2 The "Report on Operations of the Board of Higher Education Units in the New York City Veterans' Service Center", submitted to the *Board of Higher Education* at its meeting of September 23, 1946, discloses the following data regarding fields of study preferred by the veterans interviewed at 500 Park Ave., N. Y. Service Center:

| | 10,000 Veterans to June 1 | 2,459 Veterans June 1–Aug. 31 |
|---|---|---|
| Engineering | 28% | 25% |
| Business Administration | 24% | 24% |
| Liberal Arts | 14% | 20% |
| All other fields together | 34% | 31% |
| | 100% | 100% |

See, also, "Education for the Accounting Profession", by James W. DeVault. *The New York Certified Public Accountant*, August, 1945, p. 413.

3 *The New York Times* (Editorial), February 12, 1945.

4 *Democratic Education*, by Benjamin Fine. New York: Thomas Y. Crowell Co., 1945. Pages 178-9.

5 *The New York Sun*, March 10, 1945.

6 *Fortune*, April, 1945; *New York Herald Tribune*, April 5, and 12, 1945.

The Hunter College student poll indicated that 500 selected residents of New York believed that the municipal college system (1) should prepare for a job—23%; (2) should furnish a cultural education—8%; (3) should do both—65%. (4) Only 4% had no opinion.[7]

An alumni committee of one of our great liberal arts colleges, in studying its post-war function, reported that in order to prepare a student for mature participation in the society in which he lives, it was both conceivable and desirable that some vocational motivation be introduced, especially in the last two years.[8]

These are clear indications from all ages and walks of life of a popular and democratic demand for the kind of college education that will combine cultural and technical training. Indeed, one of our leading educators observed that there must be no dichotomy between the technical and the cultural, for the reason that neither has meaning without the other. A truly liberal education, Dr. Klapper said, is a balanced education which helps us to conceive the idea of a free life and gives us the power to attain it.[9]

The modern collegiate school of business is in a unique position to meet the requirements of this need, for it is so constituted as to maintain the proper balance between the liberal arts tradition and the specific requirements of preparation for a professional career in any of the various phases of business activity.[10]

In terms of types of curriculum structure for such a school, I would favor the "diagonal" plan, as recently described by Professor Boyd,[11] wherein the student begins his studies with a program containing a preponderance of subjects in the liberal arts division and a sprinkling of business subjects. As he continues through his collegiate career the trend is reversed so that, in his senior year, the student is pursuing a heavy concentration in his specialization group together with a light general elective program.

The general advantages of this plan are (1) the problem of articulation between high school and college is thereby minimized; (2) the student is introduced to business in broad terms through a general survey of business structure, organization, procedures, and laws,—all of which are basically related to the accounting process[12]; (3) the general business subjects are appropriately introduced before specialization is begun; and (4) the choice of a specialty is deferred until such a time as the student has surveyed generally the various fields of business endeavor.

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7 *The New York Sun*, July 28, 1945.

8 *Amherst Tomorrow*, A Report of the Alumni Committee on Post-War Amherst College; *Amherst Alumni Council News*, February, 1945, page 52.

See, also, the observations of Dr. Ordway Tead on the subject of curriculum in his *Annual Report*, as Chairman of the Board of Higher Education of the City of New York, for the year ended June 30, 1945: "New Opportunities on Our City Campus (1944-45)", page 23. Likewise, his "Bridging the Gulf Between Liberal and Vocational Education", *Bulletin No. 5, Board of Higher Education of the City of New York*, November 22, 1945.

9 Paul Klapper, in his *Centenary Address* entitled, "Education: A Transition", in the series on "Moral and Spiritual Foundations for the World of Tomorrow", delivered at Temple Emanu-El, New York, N. Y., January 28, 1945.

10 In "The Question of Staff Training", *The Accounting Review*, January, 1946, Raymond G. Ankers, Personnel Manager of Lybrand, Ross Bros. and Montgomery, said that, ". . . at the outset of World War II and thenceforth on, most of the public accounting firms seek only graduates of schools of commerce who have completed a four year course of study including both cultural and technical subjects."

11 "A Suggested Program for College Training in Accountancy", by Ralph L. Boyd. *The Accounting Review*, January, 1946. See, also, "College Training for Industrial Accounting", by Stanley A. Pressler. *N.A.C.A. Bulletin*, July 1, 1946.

12 "Education for Public Accounting on the Collegiate Level", by Hiram T. Scovill. *The Accounting Review*, July, 1946.

From the specific viewpoint of education for *public* accountancy, this form of curriculum design (i.e., the "diagonal" type) permits the accountancy student to defer his decision to prepare for this particular phase of the field until he has virtually completed his specialization group and has been "exposed" to the various areas of possible professional interest in the general field of accountancy.

I turn now to the expression of these general ideas in terms of specific curricular aims and objectives:

Part 1 of the tabulation which follows states those aims which pertain to the development, disciplining and harmonizing of the student's general interests, a vital part of the curriculum since all professional training must be based on a broad, liberal education. Nor am I concerned with the expression of these objectives in terms of specific course offerings or their measurement in terms of either semester hours or college credits. That will follow naturally and easily once these aims and objectives are recognized as valid. But I am concerned that, irrespective of whatever is evolved in this connection, the development and administration be along the lines of the broad divisional groupings that will be indicated, rather than within the narrow confines of the compartmentalized structure of the traditional department.[13] Approximately one-half of the curriculum should be apportioned to the area considered in Part 1.

Part 2 deals with the objectives of the offerings denominated general business education, to which I would allot one-fourth of the total program of study.

Part 3 states the aims and objectives of the specialized training that I would require of all candidates preparing for careers in public accounting. In my opinion, approximately one-fourth of the total offerings should also be required under this heading.[14]

## PROPOSED OBJECTIVES of a COLLEGE CURRICULUM FOR THE TRAINING OF PUBLIC ACCOUNTANTS

### Part 1: SPECIFIC AIMS OF THE BASIC CULTURAL EDUCATION[15]

> "That man has had a liberal education who has been so trained in youth that his body is the ready servant of his will; whose intellect is like a clear, cold, logic engine, ready to be turned to any kind of work and spin the gossamers as well as forge the anchors of the mind; whose mind is stored with a knowledge of the great and fundamental truths of Nature; one who is full of life and fire but whose passions are trained to come to heel by a vigorous will; who has learned to love all beauty, to hate all vileness, and to respect others as himself."
>
> THOMAS HUXLEY

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13 "The high degree of departmentalization of curricula accounts for the large areas of darkness to which many students seem destined today. This specialization of knowledge results in highly segregated subjects presented to the student as the mature scholars organize their content. The young student lives an intellectual day that consists of seemingly unrelated activities. He goes from history to mathematics, from mathematics to English, from English to political science, from political science to physics, and so on to other water-tight compartments of knowledge. His school or college day does not possess the unity of life as he sees it and lives it."—Paul Klapper, "Education: A Transition", *supra.*

14 Professor Boyd would also require 25%—"A Suggested Program for College Training in Accountancy", *supra;* while Dean Scovill would prescribe 27% in this connection—"Education for Public Accounting on the Collegiate Level", *supra.*

15 Not everyone will necessarily accept the five major classifications into which I have divided the field of the student's general education. Nor do these indicated groupings yield mutually exclusive categories; there is admittedly some overlapping. Furthermore, the tabulation of aims and objectives within each group is intended to be suggestive rather than complete and conclusive.

"The process of education is essentially a mode of mental living that prepares us to meet change with courage and understanding."

PAUL KLAPPER

"I fight . . . because I have a mind, a mind which has been trained in a free school to accept or to reject, to ponder and to weigh—a mind which knows the flowing stream of thought, not the stagnant swamp of blind obedience; a mind schooled to think for itself, to be curious, skeptical, to analyze, to formulate and to express its opinions; a mind capable of digesting the intellectual food it receives from a free press—because if a mind does not think it is the brain of a slave."

CORPORAL JACK J. ZUROFSKY

I. **THE BASIC TOOL OF KNOWLEDGE AND COMMUNICATION:**

*(Language)*

*The student must be adequately trained in effective methods of communication.*

1. Knowledge and command of correct patterns of speech, voice and gesture; of proper syntax, rhetoric and usage; and of a comprehensive, expressive and forceful vocabulary.

2. Skill in the effective, accurate and logical organization and arrangement of thoughts and ideas.

3. Ability to speak clearly, continuously, pleasantly, and effectively.

4. Ability to write letters, reports, etc., accurately, logically, interestingly, effectively, and with originality and facility of expression.

5. Knowledge of modern foreign language to an extent sufficient to maintain basic communication in it.

NOTE: Art and Music are, of course, also considered to be means of communication. I have preferred to include them under Part II.

II. **MAN AS AN INDIVIDUAL:**

*(Literature, Art & Music)*

*The student must be adequately trained in esthetics and humanistics as the foundation for an intelligent and satisfying mode of individual life.*

1. Knowledge of the great literature of our language and culture; also, of comparative literature, based upon knowledge of other languages and their literatures.
2. Understanding of art and music sufficient to provide the basis for their appreciation and enjoyment, as well as for skill in performance.
3. Development of attitudes and habits basic to all appreciation and enjoyment.
4. Appreciation of the values inherent in recorded human thoughts and ideals.

III. **MAN IN RELATION TO HIS SOCIAL WORLD:**

*(The Social Studies)*

*The student must be adequately trained for intelligent and harmonious participation in group activities and relationships.*

1. Knowledge and understanding of the nature of our social order; of the existence of problems therein and of the basis and nature thereof; of the importance of their solution, and of the responsibility of the individual and the group for their solution.
2. Understanding of the nature, operation and historical development of our economic, social, legal, political and educational institutions.
3. Knowledge of the duties, obligations and responsibilities of the alert and intelligent citizen.
4. Development of an individual attitude towards a comprehensive outlook in life.

5. Appreciation of moral values and their application to modes of conduct.
6. Understanding of the factors of human nature, behavior and experience affecting the individual as a personality and as a member of a social group.
7. Knowledge of the importance of collecting data; ability to subject data to appropriate statistical procedures, to interpret data and to make valid judgments based thereon.

IV. **MAN IN RELATION TO HIS PHYSICAL WORLD:**

*(Science and Mathematics)*

*The student must be adequately trained in the scheme of nature and Man's place therein; in the habit of critical, disciplined observation and thought—the scientific method.*

1. Recognition of the need for and the classification of scientific knowledge.
2. Knowledge and understanding of the evolution, growth, structure and function of living things; of the effect of chemistry upon our life and civilization; of the nature and operation of the physical universe; of the effect of earth phenomena upon modern civilization and politics.
3. Acquisition of the techniques, methods and theories basic to such knowledge and understanding.
4. Knowledge of the extent to which mathematics is basic to our existence and progress; of the extent of mathematical knowledge, theories and hypotheses. Skill in making absolute or approximate computations.
5. Development of the habit of critical, consecutive, disciplined thought based on tested fact.

V. **MAN IN RELATION TO HIS PHYSICAL AND MENTAL STABILITY:**

*(Health, Recreation and Guidance)*

*The student must be adequately trained in the development of wholesome physical habits and ideals, and of desirable mental attitudes.*

1. Knowledge of what is good health, proper organic growth and development; of relationship of efficient functioning to good health.
2. Acquisition of wholesome, permanent, constructive health, nutrition and recreational habits necessary to maintain individual and community health.
3. Development of traits of student leadership through participation in group activities.
4. Knowledge and understanding of the nature, emergence, structure, growth and development of the adult personality; and of the importance of proper and effective personality characteristics and social skills in business, civic, and social life.
5. Knowledge and understanding of the nature and importance of the ethical and spiritual values in all life.
6. Knowledge and understanding of professional and vocational requirements and opportunities and of desirable aptitudes basic to the various fields of work.

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"Liberal materials and purposes do not end abruptly where the vocation or profession begins."

J. Hugh Jackson

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Part 2: **SPECIFIC AIMS OF GENERAL BUSINESS EDUCATION**

"Business education should attempt to define the public interest, to describe going operations, to impart a clear sense of the several functional responsibilities

necessary to the conduct of economic life, to appraise the contemporary operation of these functions critically and to think creatively about their improvement."

ORDWAY TEAD

I. **INTERNAL BUSINESS RELATIONSHIPS:**

*The student must be adequately trained to know and understand the internal affairs of a business organization.*

A. *From the Viewpoint of Function:*

1. Knowledge and understanding of purchasing, materials control, and production methods and administration.
2. Knowledge and understanding of the function and scope of the enterprise's markets, wholesale and/or retail, as well as of the administration of the related functional divisions.
3. Knowledge and understanding of the business' sources of financial supply and their operation, as well as of the administration of its investments, credits and collections, and finances.
4. Knowledge, understanding and appreciation of the inter-relationship of the foregoing, the risks and risk-bearing connected therewith, the personnel and public relations problems inherent therein, and the information and reports required for proper administration, management, and operation thereof.

B. *From the Viewpoint of Structure* (Levels of management):

1. Knowledge, understanding, techniques and skills basic to the ability to determine broad governing policies. (Administration.)
2. Knowledge, understanding, techniques and skills basic to the ability to determine operating policies and control operations. (Management.)
3. Knowledge, understanding, techniques and skills basic to the ability to carry out operating policies. (Operation.)

II. **EXTERNAL BUSINESS RELATIONSHIPS:**

*The student must be adequately trained to know and understand the external relationships of a business organization.*

1. Knowledge and understanding of the growth, development, and evolution of American economic life and institutions.
2. Knowledge and recognition of the influence and importance of factors of geographic environment, both domestic and foreign.
3. Appreciation of the effect of business law and customs, upon the validity of transactions, together with relevant financial implications.
4. Knowledge and understanding of the political, financing, purchasing, marketing and other factors peculiar to foreign trade.

III. **METHODS OF MEASURING, INTERPRETING AND CONTROLLING BUSINESS ACTIVITY:**

*The student must be adequately trained to know and understand the basic methods of measuring, interpreting and controlling all business activities.*

1. Knowledge and understanding of the basic principles, methods and techniques involved in collecting, compiling, tabulating, treating, presenting and interpreting statistical data.
2. Knowledge and understanding of the basic principles, methods and techniques involved in the preparation of financial reports and statements, their analysis and interpretation, and the measurement of accomplishment reported as disclosed by their comparison with budgeted forecasts and pre-

determined standards of performance.

Part 3: **SPECIFIC AIMS OF THE SPECIALIZED TRAINING FOR PUBLIC ACCOUNTANCY**

". . . the employing accountant of today expects men to have a technical background, a sound training in accounting and related subjects."

AMERICAN INSTITUTE OF ACCOUNTANTS

I. **ACCOUNTING THEORY AND PRACTICE:**

*The student must be adequately trained to know, understand and apply the principles of accounting theory and practice.*

1. Knowledge and understanding of the principles of account keeping.
2. Ability to apply these principles to the recording of business transactions at all levels of complexity for all forms of business organization, and to the reporting of the results.
3. Recognition of the need for consistency in the application of these principles to all events occurring within a reporting period, as well as to those of successive periods.

II. **CONSTRUCTIVE ACCOUNTING:**

*The student must be adequately trained to know, understand and apply the principles involved in the design, construction, installation and revision of an accounting system.*

1. Knowledge and appreciation of the function of the accounting system as a part of the entire process of accounting.
2. Knowledge and understanding of the principles and procedures basic to the design, construction, installation and revision of an accounting system.
3. Knowledge and understanding of the function and use of mechanical devices and methods in this connection.
4. Skill and ability to apply this knowledge and understanding to specific situations.
5. Appreciation of the importance of the accounting system as a basic element in the conduct of an audit.

III. **ANALYTICAL ACCOUNTING:**

*The student must be adequately trained to know, understand and apply the principles and practices of financial statement analysis, cost accounting and budgeting.*

1. Appreciation of the value of and need for acceptable principles and techniques of accounting statement analysis.
2. Knowledge of existing methods of financial statement analysis.
3. Understanding of the extent of their statistical validity, as well as of any limitations upon their proper use.
4. Skill in the reporting and interpretation of the results of such analysis, including the meaning of the data presented in the financial statements; the significance of the balances, proportions, trends and tendencies disclosed therein; the nature and extent of any departures from predetermined forecasts and standards; etc.
5. Recognition of the importance of cost accounting and budgeting in relation to and as a means of furthering and extending accounting analysis and control.
6. Knowledge and understanding of the principles and procedures basic to the methodology of cost accounting and budgeting.
7. Ability to apply them to all functions (production, distribution, financing and administration) of all forms of business organiza-

tion (manufacturing continuously or to order, trading, etc.).

8. Knowledge and understanding of the use of cost accounting and budgeting procedures as a means of standardization and control.
9. Skill in the reporting and interpretation of the cost and budgetary data.

IV. **AUDITING:**

*The student must be adequately trained to know, understand and apply the principles, practices and standards involved in auditing and reporting.*

1. Recognition of the need for and the use of the results of the auditing process as an element of business operation, management and administration.
2. Understanding of the purposes, advantages and limitations of the various types of audit.
3. Knowledge and appreciation of the various professional and ethical responsibilities and legal liabilities which accompany and/or grow out of the work of the auditor.
4. Knowledge and recognition of the nature and statistical validity of the testing (sampling) methodology in general, and in the conduct of an audit, in particular.
5. Understanding of the effect of the existing system of internal check and control upon the correctness and integrity of the accounts maintained thereunder.
6. Knowledge and understanding of, and skill in the application, performance and use of the accepted auditing processes, techniques and standards, leading to the development of all types of auditing evidence.
7. Understanding of the nature and probative value of all types of auditing evidence, whether derived from external or internal sources.
8. Knowledge of and skill in the methods of determining the degree of credibility to be accorded such auditing evidence.
9. Knowledge of the standards of business law, procedures and conduct against which auditing evidence must be tested to determine the validity of transactions, together with any relevant financial implications.
10. Skill in the techniques of recording, classifying, collating and filing auditing evidence in the working paper file.
11. Recognition of the need for and skill in the development of the means of planning, controlling and reviewing an audit engagement.
12. Appreciation of the importance of the qualities of integrity and independence in connection with the presentation of the auditor's findings.
13. Skill in reporting upon the results of an audit engagement, whether orally or in writing.
14. Understanding of the organizational structure and functioning of the office of the independent public accountant.

NOTE: A complete and thorough knowledge of the principles and practices of accounting, as hereinabove discussed, is presupposed before instruction in auditing is begun.

V. **TAXATION:**

*The student must be adequately trained to prepare required tax reports in accordance with accepted accounting principles and governing legal precepts.*

1. Appreciation of the nature and importance of the function of taxation (federal, state and local) in our economy.

2. Knowledge and understanding of various tax laws, regulations, rulings, decisions and discussions, basic to the proper preparation of the various tax reports required to be filed by clients with the various taxing authorities.
3. Ability to recognize situations that may involve or be complicated by the present tax problems.
4. Knowledge, skill and ability involved in the preparation of the various tax returns and the determination of the tax liability shown to be due thereon.
5. Skill in the preparation and filing of all working papers necessary to support each such tax return.
6. Knowledge, skill and ability involved in sustaining the correctness of a tax report upon a subsequent review thereof.

VI. **SPECIALIZED FORMS OF ACCOUNTING:**

*The student should be adequately trained in a few forms of specialized accounting.*

1. Knowledge and appreciation of the specific nature of the organizational structure and mode of operation of the particular form of business enterprise or entity involved.
2. Knowledge of all laws and customs which may exercise an influence or regulating effect upon the business enterprise or entity.
3. Knowledge and understanding of the specific accounting system, procedures, reports, etc., required by the administrative management of such business enterprise or entity.

NOTE: It is my opinion that no attempt should be made to include instruction in more than a few forms of specialized accounting (of which Governmental Accounting, Fiduciary Accounting, and Stock Brokerage Accounting are examples) in the program of study of any particular student. Any such offering should be scheduled as a terminal course.

VII. **UNDERGRADUATE ACCOUNTING INTERNSHIP:**

*The student should, if possible and feasible, receive some supervised contact with actual public accounting practice.*

1. Organization of the knowledge, understanding, attitudes and skills produced by actual contact with auditing work in real situations.
2. Knowledge and appreciation of the problems, task, methods and techniques encountered and employed by public accountants in active practice.
3. Knowledge of the organizational structure and functioning of the public accountant's office.
4. Enlarged understanding and appreciation of the theoretical aspects of the student's studies necessarily arising from the foregoing.

NOTE: It is to be observed at the outset that this form of educational experience needs the most careful planning and the closest supervision, lest it develop into a sheer waste of time for all concerned. The advance planning should carefully delimit the precise area and level of the field of experience which it is desirable for the student to explore during his internship, as well as specify the time allocations involved therein. The supervision should be carried out by an instructor possessing a sufficiently balanced background of theory and practice to enable him to guide, evaluate and improve the results in any individual case. The entire program must, of course, be carefully integrated with the other instructional work.

Although the curriculum is a very

important element in the educational process, it is by no means the only one. Proper planning for higher education in public accountancy involves consideration of at least three other factors which I shall touch on but very briefly herein. They are: the selection of students, the qualifications of the professional faculty, and the materials of instruction and teaching methods.

Because of the relatively greater success achieved by independent practitioners of public accounting during recent years[16] and more particularly during the war period, and further, because of the exceptional "transferability" inherent in competence and achievement in this field, an abnormally large rise in enrollment for accountancy study has developed. It is sincerely to be hoped that the studies on student selection presently in progress under the aegis of the American Institute of Accountants, will help to solve this problem by eliminating unqualified students from this course of study as early in their careers as is consistent with accurate forecasting.

It is my opinion that the successful college teacher of accounting must be more than a competent professional specialist constantly in contact with the theory and practice in his field. He must have common cultural bonds with other educated persons. He must also possess the rare ability to teach, and thus facilitate the student's absorption of information, knowledge, principles and relationships as well as his acquisition of skills, attitudes, interests and ideals. He must be sufficiently alert and stimulating to pace the bright student, as well as patient and understanding enough to encourage the stragglers. That is not an easy order to fill these days, particularly in the light of the attractive offers which such men are known to receive from other sources.

Lastly, I cannot resist the temptation to express just a few thoughts upon a phase of the subject which, strangely enough, is rarely commented upon in this connection. I refer to the materials of instruction and methods of teaching. I venture to say while most accounting texts at the college level are sound enough from the viewpoint of accuracy of content and adequacy of coverage, many of them would not meet the rigid standards of pedagogical excellence prescribed for textbooks at the lower educational levels. Too often, indeed, is the subject "thrown at" a college student-reader for him to puzzle out the connective tissue of unstated reasoning! Too rarely does one find the planned use of teaching methods and devices at the college level.[17] For example, we have lagged woefully in the use of modern audio-visual methods and aids as a means of presenting to the student the nearest thing to actual experience with realities.

The college teachers of accounting are on a threshold of an era that offers them the greatest challenge since the beginnings of our profession. Let us hope that our thinking, our planning and our actions are all equal to the opportunity that now confronts us!

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16 "Income From Independent Professional Practice", by Milton Friedman and Simon Kuznets, New York: *National Bureau of Economic Research,* 1945. See review in *The New York Certified Public Accountant,* April, 1946, page 205.

17 I wonder how many college teachers of accounting are familiar with such a book as "*College Teaching (Its Rationale)*" by Theodore H. Eaton. New York: John Wiley & Sons, Inc., 1932. Or, "*The Training of College Teachers*",—William S. Gray, Editor. Vol. II of The Proceedings of The Institute For Administrative Officers of Higher Education. The University of Chicago Press. Chicago, 1930.

# CORRESPONDENCE

*To the Editor of the New York Certified Public Accountant:*

I noted with interest Mr. Seidman's letter in the August, 1946, issue in the "Correspondence" section. In criticizing Mr. Stephen Chan's article "The Supervision and Review of Accounting Engagements", Mr. Seidman says in item 6 that "sufficiency or insufficiency of coverage (insurance) is not a function within the accountant's province unless he also holds himself out as an insurance expert." The rest of the paragraph is further embellishment on the same theme.

I question the propriety of this conclusion, especially in view of the ever-increasing responsibilities of the accountant to the client and to outside interests. I have always considered a review of insurance coverage an important auditing step not only from the point of view of advising the client of insufficiency but also in commenting on this point in financial reports.

If I am wrong I wish someone would confirm it. Being lazy by nature, I shall be pleased to divest myself of an alleged responsibility.

Very truly yours,

BENJAMIN M. SIEGEL

August 28, 1946
New York, N. Y.

*To the Editor of the New York Certified Public Accountant:*

I fell behind in reading the New York Certified Public Accountant while I was in service, and so have just read the July, 1946, issue. I was interested in Mr. Gruneberg's "reply" to Mr. Lieberman's article on "Two Tax Systems".

Mr. Gruneberg notes that English barristers are never required to report on the accrual basis for tax purposes. The reason is, strangely enough, that they have nothing to accrue.

Stemming from ancient times is the rule that barristers have no right to bill their clients for fees but are strictly dependent on "gifts" from the latter based, presumably, on the friendly feeling resulting from seeing a good job well done. The "hood" on their gowns is reported to be designed as a receptacle for such "gifts" and to be placed on his back so that the barrister may not even know to whom he owes his thanks for the "gift".

It is apparent, then, that a barrister has no income to accrue and must needs report his receipts on a cash basis.

Very truly yours,

RALPH G. LEDLEY

September 4, 1946
New York, N. Y.

# BOOK REVIEWS

**Commercial Law Questions,**

Edited by Wallace D. Cathcart. San Francisco, Calif., PACIOLI PRESS, 1946. 74 pages. $2.00.

This is the first text offered by Pacioli Press, which plans a series to be devoted to professional accountancy and education therein. It is designed as an aid to candidates who are engaged in reviewing the subject of Commercial Law, with particular emphasis upon the C.P.A. examination in that subject.

The introduction to this work contains the author's suggestions for review as well as his recommendations as to the best methods to be pursued by candidates in preparing answers to the examination in Commercial Law. There is also included the Suggestions to Candidates for Commercial Law Examinations, prepared by the Board of Examiners of the American Institute of Accountants. Both sets of suggestions will be an invaluable aid to candidates in this field.

The questions are developed in fifteen groupings and the plan is to state at the beginning of each section a bibliography of standard commercial law text materials, to be utilized by the candidate in reviewing the subject matter of the section.

Following this bibliography there is reproduced a series of questions from the standard C.P.A. examinations of the American Institute of Accountants (225, in all), designed to test the adequacy of the prescribed review.

The materials contained in this volume have been used for the past fifteen years in the Graduate School of Accountancy of Golden Gate College in San Francisco, and the editor indicates that during that period practically all of the candidates who have used these materials have passed the Certified Public Accountant examination in Commercial Law.

E. S.

**Auditing Questions from the Professional Examinations,**

With Comments On Selected Cases and Subjects, by Myron M. Strain. San Francisco, Calif., PACIOLI PRESS, 1946. 159 pages. $3.00.

This is another text in the series by Pacioli Press. It was originally prepared as an aid to the review of Auditing by C.P.A. examination candidates and the included materials were employed for the purpose for the last fifteen years in the Graduate School of Accountancy of Golden Gate College in San Francisco, where the author is the Dean.

Twelve fields of activity under the general heading of Auditing have been developed in this book. There is, first, a commentary by the author which includes an elaborate description with the respect to the development of contemporary auditing standards, concepts, terminology and report practice, as well as an analysis of the relevant methods of verification and numerous discussions of controversial or obscure points, together with bibliographical notes.

Specimen programs for the verification of eight separate balance sheet and income items are included, together with specimen answers to examination questions. Both of these are intended to extend the scope of the comment section and to provide tangible suggestions to candidates as to the form of answers to examination questions.

Additional questions without comments have been appended to each section for the purpose of providing the basis for classroom discussion and to afford the candidate new material upon which to test the adequacy of his review.

E. S.

**Arbitration of Labor Disputes,**

by Clarence M. Updegraff and Whitley P. McCoy. COMMERCE CLEARING HOUSE, INC., New York, 1946. 291 pages. $3.75.

In this book the authors—to use their own words—"have, with some misgivings, undertaken the rather ambitious task of attempting . . . to accomplish two objectives: (1) an exposition of the law of arbitration, as applied particularly to labor disputes, with citations to the authorities, to serve as useful reference work for lawyers; and (2) a practical and not-too-technical guide for the layman who may be called upon to conduct an arbitration without benefit of legal counsel." Within these self-imposed limits, they have written a useful book. The attitude of the courts on such matters as the selection of arbitrators, the agreement to arbitrate and the submission, procedure, the form and validity of awards and enforcement of contracts to arbitrate, for example, is discussed. The chapter on procedure also contains some useful hints on how to conduct a hearing which should be helpful to the uninitiated.

The authors would undoubtedly be the first to point out that more than an understanding of labor law or of correct procedure is necessary if arbitration, as a means of settling labor disputes, is to succeed. Knowledge of these things is essential but is no guarantee that a person will make a good arbitrator any more than familiarity with a book of rules on football insures a winning team. In the last analysis, it is the nature of the decision rendered, within the rules of the game, which determines whether arbitration will be a positive force in any machinery for resolving industrial disputes. In a short chapter of less than nine full pages the authors review certain commonly recurring types of cases arbitrated "with some occasional indication of the considerations which frequently guide arbitrators in their disposition." It is to be hoped that someone will attempt to set forth a comprehensive discussion of the considerations which influence arbitrators in making decisions, a subject admittedly not within the scope of the present book.

It is only natural for the authors, who are both professors of law, one at the State University of Iowa and the other at the University of Alabama, to be favorably inclined to the legal profession. Insofar as the presentation of cases is concerned, they state, "The safest rule would be to retain a lawyer in all cases, primarily to give advice as to whether the case be handled by a lawyer, and secondarily to present the case to the arbitrator if he thinks it advisable." With regard to the arbitrator, they again lean heavily on lawyers or men with considerable legal training, conceding however, that there have been a few notable exceptions of successful arbitrators "who have had no legal experience beyond that gained in holding arbitration proceedings where the parties are represented by attorneys." The reviewer ventures the suggestion that perhaps it is men of the type included in the exceptions, presumably such famous arbitrators as George W. Taylor and William Leiserson, who are most urgently needed for the important role of arbitrators. To view the field of arbitration as primarily within the province of the legal profession—with the door left open slightly for the admission of a few who cannot practice before the bar, is to confuse the form for the substance of arbitration.

THOMAS L. NORTON

The School of Business and Civic Administration

The City College of New York.

**Allocation of Income in State Taxation,**

by George T. Altman and Frank M. Keesling, Commerce Clearing House, Inc., Chicago and New York, 1946. 263 pages, $4.00.

Taxpayers deriving income from property or activities extending into more than one state are confronted with a problem of determining the income allocable to any state for income tax purposes. The problem does not arise where an individual taxpayer is a resident of a state which taxes residents on their income irrespective of its source. It does arise, however, in the case of non-residents and in the case of residents of states which confine their tax on income to income from sources within the state. The problem also arises in the case of estates and trusts, with complicated effects in situations where the decedent or grantor was domiciled in one state, the fiduciary in another, and the beneficiaries in still a third. Where the taxpayer is a corporation carrying on activities in more than one state, the problems of allocation can be particularly baffling.

When it is considered that 29 states and the District of Columbia tax incomes of individuals, estates, and trusts, and 32 states and the District impose a tax upon corporate income, each under a different law and each applying different rules of allocation, it becomes apparent that overlapping in allocation and conflicting jurisdictional claims will result.

In this book the authors have carefully explained the principles applied and methods used in determining what portion of income each state can and does tax. The different problems of allocation which have arisen and which are likely to arise are discussed fully and the policies and practices of the various states relating thereto are thoroughly analyzed with comments on the appropriate court decisions. The authors vividly point out by many examples the possibilities of double and multiple taxation on the one hand, and complete or partial escape from taxation on the other.

The authors also analyze the problems of deductions from income in arriving at the base income to be attributed to the taxing state. They discuss the problems relating to credits allowed for taxes paid other states, and explain the theory and practice of computing interdependent taxes, with detailed illustrations. The discussion of the different problems in allocation, which is interestingly presented, is indicated by the following chapter headings: Nature and Importance of Allocation, Constitutional Limitations, Allocation According to Domicile and Residence, Specific Allocation According to Source, Principles of Allocation of Business Income, Theory of the Apportionment Formula, and Allocation Formulae in Practice.

This book will be found to be a valuable tool for those confronted with the problem of determining the allocation or income, either for a corporation or an individual, under any state income tax law.

In view of the slow progress that has been made in the effort to achieve uniformity by the educational process, the suggestion of the authors of a plan to compel "uniformity of method and avoidance of overlapping" in allocating income through federal legislation is a dynamic one and it makes interesting reading. This thought it very appealing and any plan that would bring to an end the confusion and inequities resulting from the present situation is, indeed, an attractive one. Tax officials and tax practitioners should thoroughly discuss this, and, who knows, maybe the thing will come to pass.

N. Harry Sack

80 Broad Street,
New York, N. Y.

**Modern Practical Accounting,** Elementary and Advanced (2 volumes),

by Earl A. Saliers. Chicago, AMERICAN TECHNICAL SOCIETY, 1946. Vol. I—365 pages; Vol. II—368 pages. $3.50 each.

In two volumes comprising forty chapters and aggregating approximately seven hundred pages of textual material, Professor Saliers has produced "Modern Practical Accounting, Elementary and Advanced." With no startling innovations as to either approach or content, Volume I is begun with the usual introductory chapter on the uses of accounting, followed by the routine exposition of the balance sheet and profit and loss statement, the theory of debit and credit, the journal and ledger, mixed accounts and adjusting entries, working papers and closing entries, and the construction and interpretation of statements. Additional chapters deal with special journals and controlling accounts, business procedure and business papers, notes and drafts, corporations, partnerships, the voucher system, manufacturing accounts, statement analysis, and the problems of management.

The first two chapters of Volume II are concerned with sundry phases of partnership and corporation accounting. These are followed by chapters on financial statements, accruals and adjustments, valuation, depreciation, reserves and funds, corporations, capital stock, surplus, bonds, consolidations, analysis of comparative statements, application of funds, branches, statement of affairs, receiverships, consignments and installment sales, and applied mathematics.

Limited to the aforementioned seven hundred pages, a detailed and complete analysis of both elementary and advanced accounting is physically impossible. Only by the exclusion of certain topics and by the summary treatment of others has the text been able to overcome the physical handicaps with which it is burdened. As a result, the edition might have more appropriately been entitled "An Introduction to Modern Practical Accounting." By far, the best chapters are those devoted to background material on the uses of accounting, business procedure and business papers, partnership law and organization, and the modern corporate enterprise.

In a number of instances, valuable space has been dissipated by unnecessary repetition. For example, accrual and deferral adjusting entries are illustrated in substantially the same form no less than three times—, in Chapter 6 of Volume I and in Chapters 1 and 4 of VolumeII. Routine corporate stock entries are found in Chapter 13 of Volume I, in Chapter 2 of Volume II, and for the third time in Chapter 9 of Volume II. A more economical utilization of available space in connection with these and other topics would have allowed for the inclusion of additional subjects or a more extended analysis of those covered.

As an introduction to general accounting, Professor Saliers' work has undoubted merit. It is of especial interest to those desiring an insight into the vast field of accounting and a broad view of the myriad problems therein. The serious student of the subject, however, must look elsewhere for a more complete and a more extended exposition of both the elementary and advanced phases. Furthermore, the text is definitely limited in its application to classroom purposes by the complete absence of question and problem material, so vital in both the individual and group learning processes.

It is hoped that the author's optimism as reflected in the preface to the text is not misplaced when he writes that "rapid progress has been made during the last fifty years in establishing accounting on a professional basis. This book so reflects these developments that the student will readily understand them and be able to advance rapidly toward success in business." The undersigned fervently bids Godspeed to them all.

IRVING J. CHAYKIN

The School of Business and Civic Administration,

The City College of New York.

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